July 23, 2023

SUBMITTED VIA CFTC PORTAL
Secretary of the Commission
Office of the Secretariat
U.S. Commodity Futures Trading Commission
Three Lafayette Centre 1155 21st Street, N.W.
Washington, D.C. 20581

Re: Comments Responding to the Commission's Specific Questions Related to KalshiEX, LLC's Proposed Congressional Control Contracts

To Whom It May Concern:

KalshiEX, LLC ("Kalshi" or "Exchange") is grateful to the Commission for its consideration of Kalshi's proposed contracts. As with Kalshi's previous submission, the Exchange welcomes the opportunity to address the Commission's questions in full. Public comment is a critical tool for the Commission to engage with market participants and gauge the public's stance on issues regarding contract utility, surveillance, and viability.

The Commission is unique among financial regulators for its commitments to, and success fostering, innovative new products. As Chairman Behnam testified recently in front of the Senate Agriculture Committee,

> On September 21, 1922, nearly 100 years ago to the day, the Grain Futures Act of 1922 was signed into law, which led to the near immediate establishment of the then CFTC. With that legislative accomplishment, this Committee and the Congress swiftly responded to a policy need that arose on the heels of emerging risks to American consumers because of new financial markets and products, technological innovation, and the promise of economic development. With the CFTC's rich history overseeing commodity markets, coupled with its expertise and track record, which rests on a firm foundation as a forceful and disciplined cop on the beat, the Agency stands ready to tackle these new risks and opportunities one century later.[1]

Or as former Chairman Giancarlo wrote to the same body,

> …the CFTC has been at the forefront of US financial market innovation since the agency's inception. In fact, the CFTC was reformulated over forty years ago into an

[1] Testimony of Chairman Rostin Behnam Regarding the Legislative Hearing to Review S.4760, the Digital Commodities Consumer Protection Act at the U.S. Senate Committee on Agriculture, Nutrition, and Forestry. September 15, 2022. Available at https://www.cftc.gov/PressRoom/SpeechesTestimony/opabehnam26.

> independent body specifically to safeguard a breakthrough in financial innovation – financial futures – that enabled the global economy to hedge the risk of moving interest and exchange rates ensuring the US Dollar's primacy as the world's reserve currency. During the past decades, the CFTC has deftly overseen more new financial product innovation than almost any other market regulator. [2]

Projects like LabCFTC–now the Office of Technology Innovation–, and the continued efforts by the Commission to regulate digital asset markets, remind us of the agency's commitment to responsible innovation. Responsible innovation is in the public interest and provides market participants with hedging and price basing opportunities they would not otherwise have.

Kalshi's contract is yet another iteration of this endeavor. The contract is compliant with the law, Core Principles, rules, and regulations. It has broad hedging and price-basing utility and social value, as detailed by Kalshi's submission to the Commission and dozens of public comments from retail customers, small businesses, and leading members of industry. The Commission's decision should consider the full weight of evidence that it has been provided with, beginning with Kalshi's original submission regarding political control contracts to DMO on March 28, 2022, until today. That evidence comes from academic research, market testimony, and other election markets running in the United States and abroad. After considering all of this evidence, there is only one reasonable determination the Commission can make: that these contracts comply with the Commodity Exchange Act ("CEA") and are affirmatively advance, as the CEA's mission reminds us, the "national public interest by providing a means for managing and assuming price risks, discovering prices, or disseminating pricing information through trading in liquid, fair and financially secure trading facilities."

In these responses, the Exchange references and integrates comments from the prior submission, as well as the current one, which Kalshi strongly believes are material to this matter.

1. **Do these contracts involve, relate to, or reference gaming as described in Commission regulation 40.11(a)(1) and section 5c(c)(5)(C) of the Commodity Exchange Act, or in the alternative, involve, relate to, or reference an activity that is similar to gaming as described in Commission regulation 40.11(a)(2) and section 5c(c)(5)(C) of the Commodity Exchange Act?**

The application of the Special Rule in section 5c(c)(5)(C) of the Commodity Exchange Act ("Special Rule") is addressed at length in its original submission, including letters provided by our counsel Elie Mishory, along with former CFTC General Counsel Jonathan Marcus and

[2] Giancarlo, J. Christopher. "J. Christopher Giancarlo Letter in Support of the Digital Commodities Consumer Protection Act." September 15, 2022. Available at https://tabbforum.com/opinions/j-christopher-giancarlo-letter-in-support-of-the-digital-commodities-consumer-protection-act/.

former CFTC General Counsel Dan Davis.[3] Additional commenters on this point include former Nadex CEO Timothy McDermott, as well as other public comments by former CFTC officials and industry actors such former Commissioner Brian Quintenz, former Commissioner Mark Wetjen, "father of futures" Dr. Richard Sandor, Gregory Kuserk, who led the Product Review branch in DMO, former MPD Director Josh Sterling, Daniel Gorfine, Lewis Cohen, Jeremy Weinstein, Susquehanna International Group, Tabet DiVito & Rothstein, and Railbird Technologies.[4] Many other comments also detail the qualitative differences between the contracts proposed by Kalshi and gaming, by virtue of the contract's economic purpose. The Exchange makes the following points as well.

1: Elections and political control are not games.

Unlike games, in which the underlying activity has no inherent economic value apart from the money wagered on it, political control has an obvious and large economic impact, as it heavily influences expectations and the likelihood of public policy change. As Gregory Kuserk noted, unlike games, "Elections are events that are very important to the public, and there is a very strong public interest in having accurate data regarding elections."[5] Kalshi detailed as much in dozens of pages of evidence provided to the Commission, drawing on private and university research, policymaker and industry testimony, and the financial press.[6] Many public comments by retail, industry, and academia have confirmed as much.[7]

Kalshi's contracts do not involve gaming. It involves the partisan affiliation of the Speaker of the U.S. House of Representatives and the U.S. Senate's President *pro tempore*, which are not determined through or relate to games of chance, or games of skill.[8] Elections are not games, full stop. Indeed, the *Nadex Order* did not identify political elections themselves–the core of American democracy–as being a game.[9]

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[3] Public comment by Elie Mishory. Available at https://comments.cftc.gov/PublicComments/ViewComment.aspx?id=70781.
[4] Public comments 70786, 70771, 69687, 70754, 69737, 70755, 69736, 69723, 70743, 70765, 70752.
[5] Public comment by Gregory Kuserk. Available at https://comments.cftc.gov/PublicComments/ViewComment.aspx?id=70754.
[6] Memorandum in Support of Kalshi's Political Control Contracts, submitted to Division of Market Oversight (DMO) March 28, 2022.
[7] See public comments by Chicago Booth school Professor Michael Gibbs and Susquehanna International Group Special Counsel David Pollard. Available at https://comments.cftc.gov/PublicComments/ViewComment.aspx?id=69704 and https://comments.cftc.gov/PublicComments/ViewComment.aspx?id=70743.
[8] Kalshi's Congressional control submission, available at: https://www.cftc.gov/sites/default/files/filings/ptc/22/08/ptc082422kexdcm001.pdf. See page 9.
[9] In the Matter of the Self-Certification by North American Derivatives Exchange, Inc. of Political Event Derivatives Contracts and Related Rule Amendments under Part 40 of the Regulations of the Commodity Futures Trading Commission (April 2, 2012), available at: https://www.cftc.gov/stellent/groups/public/@rulesandproducts/documents/ifdocs/nadexorder040212.pdf.

2: Trading on Congressional control is not gaming

The *Nadex Order* asserted that gaming is equivalent to placing a wager or bet, and it cited a federal statute that defined the term bet or wager as "the staking or risking by any person of something of value upon the outcome of a contest of others."[10] If taking a position on a Congressional control contract is equivalent to a 'wager' or 'bet' because it places money on an event's outcome, that would imply that taking a position in any event contract is also equivalent to a 'wager' or 'bet'.[11] This is not true in law. While gambling is illegal in many states and interstate betting is prohibited, event contracts are legal in all jurisdictions. As former Commissioner Quintenz wrote:

> Gaming describes wagering money on an occurrence that has no inherent economic value itself other than the money wagered on its outcome. For instance, wagering money on roulette or blackjack should be considered gaming because there is no economic significance of the activity apart from the wager itself. Speculation, on the contrary, is risking value where the underlying activity has economic consequences, which then means the speculative activity creates valuable societal and economic benefit from a price-discovery and risk transfer function for those exposed to the risk of that underlying activity..[12]

The relevant language of "involve, relate to, or reference" comes from Commission regulation 40.11.[13] This language cannot be broader than the statutory language that is simply "involves".[14] By definition, if the regulation applied *more broadly* than the statute, it would per se violate the APA and be invalid.[15]

2. What role does the requirement that the contracts trade in multiples of 5000 and/or the position limits applicable to the contracts play in the analysis of whether the contracts involve, relate to, or reference gaming as described in Commission regulation 40.11(a)(1) and section 5c(c)(5)(C) of the Commodity Exchange Act? Are the position limits reasonably enforceable?

It does not play a role. A larger order size will likely reduce the number of smaller traders and trades, but does not affect the contract's hedging utility.

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[10] *Nadex Order* at 3
[11] Some commentators appear to equate speculation with gaming and do not sympathize with the important role speculation plays in price discovery and risk transfer. Many commodity futures markets, such as those in oil, often feature large amounts of speculative behavior yet clearly do not constitute "gaming" contracts.
[12] See Public Comment on Kalshi Contracts from Brian D. Quintenz, available at: https://comments.cftc.gov/PublicComments/ViewComment.aspx?id=70786
[13] 17 C.F.R. § 40.11(a)
[14] 7 U.S.C § 7a-2(c)(5)(C)
[15] Quintenz, *ErisX*.

The position limits are enforceable; Kalshi is regulated by the Commission who can monitor such behavior. Other exchanges list products with custom order sizes, notional sizes, and position limits as well. There is no reason to speculate that Kalshi will somehow not be able to enforce this. Indeed, the Division is well aware of Kalshi's ability to enforce position limits. Additionally, it is not clear why Kalshi's ability to enforce a rule is appropriate for public comment. How is a member of the public supposed to have information on Kalshi's systems and procedures and internal processes for compliance? It would seem that the most appropriate party to address this question to is Kalshi, and Kalshi notes that surprisingly and incongruously, the Commission has never asked Kalshi this question.

3. Should the Commission consider whether similar offerings are available in traditional gaming venues such as casinos or sports books and/or whether taking a position on elections or congressional control is defined as gaming under state or federal law?

1: Should the Commission consider whether similar offerings are available in traditional gaming venues such as casinos or sports books?

No, the Commission should not consider this in determining whether a contract is gaming and subject to the Special Rule for event contracts, for four reasons:

1. Presence on an illegal exchange, casino or sportsbook does not by right cause relation to gaming. For example, if corn futures become widely traded in casinos and sports books, that would not change the nature of the corn futures contract into a gaming contract. The converse is also true. If a traditional futures exchange started a roulette parlor, the bets in the parlor would still be gaming.
2. What is offered at such venues changes over time. For example, if we used this "nature of the venue determines nature of the product" standard, many commodity futures and securities might have originally been considered gaming because bucket shops traded those products in large volumes in the late 19th and early 20th centuries. They may have continued to do so in the absence of bucket shop prohibitions.
3. The Commission prevented Congressional control contracts from being listed on-exchange in the *Nadex Order*. It would be circular to use the fact that such activity has persisted off-exchange as evidence the activity is gaming. For example, if the Commission prohibited oil futures, and oil futures trading moved to casinos, that would not suddenly change the economic nature of oil futures.
4. The Commission did not consider the venues offering, for example, Bitcoin contracts prior to the listing of Bitcoin contracts on DCMs. If the Commission considered this inquiry to be dispositive that something is gaming, those contracts would be gaming contracts because of their large presence on such venues.

However, even if the Commission did consider venue as relevant in determining whether the contracts involve gaming, Congressional control is not offered on any legal American sportsbook and is not available in casinos, like those in Las Vegas.[16] Bets on the control of Congress aren't accepted at Caesar's Palace or the Bellagio. Such contracts are only currently offered on some overseas betting services, and illegal or unregulated venues in the United States.

Instead of considering venue, the Commission should consider whether the subject of the contracts involves gaming when adjudicating whether a contract involves gaming, per Kalshi's letter on the Special Rule's application.

2: Should the Commission consider taking a position on elections or congressional control is defined as gaming under state or federal law?

No, for two reasons.

First, because per the Special Rule, only the underlying event (Congressional control) should be considered in determining whether the contracts involve gaming. The application of the Special Rule with regards to this question is addressed at length in a separate comment, which also includes letters provided by our counsel, former CFTC General Counsels Jonathan Marcus and Dan Davis.[17] Additional commenters on this point include former Commissioner Brian Quintenz, former Commissioner and Acting Chairman Mark Wetjen, "father of financial futures" Dr. Richard Sandor, MPD Director Josh Sterling, our director Timothy McDermott, as well as other public comments by former CFTC officials and industry actors such as Daniel Gorfine, Lewis Cohen, Tabet DiVito & Rothstein, and Jeremy Weinstein.[18]

Second, taking a position in an event contract is not equivalent to, as states or the federal government may define it, gaming. This is not true legally (interstate betting is illegal, and betting is illegal in many states; event contracts are legal in all jurisdictions) or in practice. As then Commissioner Quintenz wrote in his *ErisX* statement,

> Whereas bettors participate in games of pure chance, whose sole purpose is to completely reward the winner and punish the loser for an outcome that would otherwise provide no economic utility (think roulette), speculators in the derivatives market participate in non-chance driven outcomes that have price forming impacts upon which legitimate businesses can hedge their activities and cash flows.[19]

[16] McIntre, David. "They Won't Take Your Bet On The Election In Las Vegas." *FiveThirtyEight*. 2016.
[17] Public comment by Elie Mishory. Available at https://comments.cftc.gov/PublicComments/ViewComment.aspx?id=70781.
[18] Public comments 70786, 69737, 69687, 70755, 69736, 70765, and 69723.
[19] See Statement of Commissioner Brian D. Quintenz on ErisX RSBIX NFL Contracts and Certain Event Contracts, "Any Given Sunday in the Futures Market" (Mar. 25, 2021), available at https://www.cftc.gov/PressRoom/SpeechesTestimony/quintenzstatement032521)

Taking a position in an event contract is also not equivalent to gaming, as defined by those laws, because such laws are not operative on CFTC-regulated products. Federal law definitions of gaming, betting, wagering carve out exemptions for CFTC-regulated products.[20] Many states' gaming provisions also include such exemptions.[21] States' gaming provisions are preempted explicitly as well by the CFMA.[22] Even derivatives products that are excluded or exempted from CFTC regulation still preempt state gaming and bucket shop laws per the CFMA.[23] It could not follow more plainly that CFTC-regulated derivatives have the same preemptive effect. Congress has repeatedly recognized that futures and other derivative contracts serve economic purposes and, therefore, state laws that purport to prohibit or regulate futures or derivative contracts (including gaming laws) do not violate the CEA and are preempted. All of this shows that Congress and the states understand that there is a critical distinction between betting and legitimate, federally recognized and regulated financial activity. Election contracts that are designed for price formation and hedging on a derivative exchange constitute legitimate financial activity. Therefore, it would be incorrect to give consideration of the definitions under state and federal gambling laws. As these laws themselves recognize, they do not apply to contracts like Kalshi's.

Indeed, a key purpose of the CEA and granting the CFTC exclusive jurisdiction over futures was to authorize and promote trading of futures contracts notwithstanding state laws that might purport to prohibit them as gambling. The only way in which state law is relevant is if the activity underlying the event contract violates state law, such as a contract on murder or state income tax evasion. In that case, Congress wanted to make sure that a futures contract would not legitimize that activity without the Commission considering whether trading the contract would be contrary to the public interest.[24]

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[20] The Unlawful Internet Gambling Enforcement Act of 2006 "do[es] not include…any transaction conducted on or subject to the rules of a registered entity or exempt board of trade under the Commodity Exchange Act". 31 U.S.C. § 5362(1)(E) (2006).

[21] For example, Washington state RCW 21.30.030 clarifies that CFTC-regulated transactions are not affected by its anti-bucket shop provisions.

[22] 7 USC 2(a)(1) covers exclusive CFTC jurisdiction over futures and swaps, so any state laws that would purport to regulate or prohibit futures or swaps would be preempted.. The CEA also preempts state gaming laws with respect to derivative products that are excluded or exempt from the CEA. *See* 7 USC 16(e)(2) ("This Act shall supersede and preempt the application of any State or local law that prohibits or regulates gaming or the operation of bucket shops . . . in the case of --- (A) an electronic trading facility excluded under section 2(e) of this Act; and (B) an agreement, contract, or transaction that is excluded from this Act under [provisions of] the Commodity Futures Modernization Act of 2000, or exempted under section 4(c) of this Act.").

[23] *Ibid*

[24] Congress obviously would not be concerned about legitimizing elections. Even if the focus comes to legitimizing the trading on elections as part of the ultimate public interest analysis, the Commission has already crossed that bridge by long permitting market participants to trade such contracts pursuant to no action letters awarded to unregulated markets. The notion that allowing a regulated exchange to offer the contracts is what changes the public interest analysis is insupportable.

As for the federal prohibition on interstate betting, the Wire Act is irrelevant here–it applies only to sports betting and wagering. Moreover, when Congress most recently addressed the intersection of gambling/gaming and the Internet, it carved out derivatives contracts (both on exchange and over the counter) from the definition of betting and wagering, thereby plainly recognizing that derivatives contracts serve economic purposes that distinguish them from gambling/gaming.[25] Congress recognized this much earlier too, granting the CFTC exclusive jurisdiction over futures as noted above and expressly preempting state gaming laws in the CFMA.[26]

Additionally, many broad state gambling laws would define all event contracts as gaming, as well as many other futures, swaps, and options. States like New Hampshire, for example, define gambling as having "to risk something of value upon a future contingent event not under one's control or influence."[27] If the Commission were to find that the contracts involve gaming on the theory that New Hampshire state law prohibit gambling/wagering on elections, that would mean "wagering" is equivalent to taking a position on any event contract, which in turn would require that the Special Rule is triggered by *any* event contract because many New Hampshire's and many other state's gambling laws prohibit wagering on the outcome of *any* future event. That interpretation was clearly not Congress' intent. Instead, Congress narrowly defined a small number of event contracts whose underlying event involves an unsavory activity that Congress did not want the CFTC to legitimize without evaluating whether trading a contract on that activity would be contrary to the public interest (as per the text, which isolates a selected set of enumerated events to target).

Time and time again, Congress and states have indicated that the Commission has the decision making power over derivatives market issues, including event contracts, and approval of Kalshi's contract has no involvement with gaming any more than an event contract on the growth of Gross Domestic Product or whether a bill becomes law. If the Commission chooses to isolate

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[25] The Unlawful Internet Gambling Enforcement Act of 2006 "do[es] not include…any transaction conducted on or subject to the rules of a registered entity or exempt board of trade under the Commodity Exchange Act". 31 U.S.C. § 5362(1)(E) (2006).

[26] 7 USC 2(a)(1) covers exclusive CFTC jurisdiction over futures and swaps, so any state laws that would purport to regulate or prohibit futures or swaps would be preempted.. The CEA also preempts state gaming laws with respect to derivative products that are excluded or exempt from the CEA. *See* 7 USC 16(e)(2) ("This Act shall supersede and preempt the application of any State or local law that prohibits or regulates gaming or the operation of bucket shops . . . in the case of --- (A) an electronic trading facility excluded under section 2(e) of this Act; and (B) an agreement, contract, or transaction that is excluded from this Act under [provisions of] the Commodity Futures Modernization Act of 2000, or exempted under section 4(c) of this Act.").

[27] New Hampshire Rev Stat § 647:2(II)(d) (2017); see also Alaska Stat. § 11.66.280(3) ("gambling" means that a person stakes or risks something of value upon the outcome of a contest of chance or a future contingent event not under the person's control or influence, upon an agreement or understanding that that person or someone else will receive something of value in the event of a certain outcome"); Oregon Rev. Stat. § 167.117(7) ("'Gambling' means that a person stakes or risks something of value upon the outcome of a contests of chance or a future contingent event not under the control or influence of the person . . .").

these contracts as involving gaming but not those many others, it would be acting contrary to Commission precedent and in an arbitrary way.

4. Do these contracts involve, relate to, or reference "an activity that is unlawful under any State or Federal law" as described in Commission regulation 40.11(a)(1) and section 5c(c)(5)(C) of the Commodity Exchange Act?

No. The contracts solely involve the partisan affiliation of the Speaker of the U.S. House of Representatives and the President *pro tempore* of the U.S. Senate.

The contracts also do not involve unlawful activity because of state prohibitions against election 'wagering' or 'betting', or federal laws prohibiting interstate 'betting'. Two arguments below explain why.

First, because per the Special Rule, only the underlying event (Congressional control) should be considered in determining whether the contracts involve gaming. The application of the Special Rule with regards to this question is addressed at length in a separate comment, which also includes letters provided by our counsel, former CFTC General Counsels Jonathan Marcus and Dan Davis.[28] Additional commenters on the matter include former MPD Director Josh Sterling, our director Timothy McDermott, as well as other public comments by former CFTC officials and industry actors such as Daniel Gorfine, Lewis Cohen, Tabet DiVito & Rothstein, and Jeremy Weinstein.[29]

Second, taking a position in an event contract is not equivalent to, as states or the federal government may define it, 'wagering' or 'betting' which they prohibit. This is not true legally (interstate betting is illegal, and betting is illegal in many states; event contracts are legal in all jurisdictions) or in practice.

Taking a position in an event contract is also not equivalent to the unlawful activity such laws refer to, because such laws are not operative on CFTC-regulated products. Federal law definitions of gaming, betting, wagering carve out exemptions for CFTC-regulated products.[30] Many states' gaming provisions also include such exemptions.[31] States' gaming provisions are preempted explicitly as well by the CFMA.[32] Even derivatives products that are excluded or

[28] Public comment by Elie Mishory. Available at https://comments.cftc.gov/PublicComments/ViewComment.aspx?id=70781.
[29] Public comments 69737, 69687, 70755, 69736, 70765, and 69723.
[30] The Unlawful Internet Gambling Enforcement Act of 2006 "do[es] not include…any transaction conducted on or subject to the rules of a registered entity or exempt board of trade under the Commodity Exchange Act". 31 U.S.C. § 5362(1)(E) (2006).
[31] For example, Washington state RCW 21.30.030 clarifies that CFTC-regulated transactions are not affected by its anti-bucket shop provisions.
[32] 7 USC 2(a)(1) covers exclusive CFTC jurisdiction over futures and swaps, so any state laws that would purport to regulate or prohibit futures or swaps would be preempted.. The CEA also preempts state gaming laws with respect

exempted from CFTC regulation still preempt state gaming and bucket shop laws per the CFMA.[33] It could not follow more plainly that CFTC-regulated derivatives have the same preemptive effect. Congress has repeatedly recognized that futures and other derivative contracts serve economic purposes and, therefore, state laws that purport to prohibit or regulate futures or derivative contracts (including gaming laws) do not violate the CEA and are preempted. All of this shows that Congress and the states understand that there is a critical distinction between betting and legitimate financial activity. Election contracts that are designed for hedging on a financial market constitute legitimate financial activity. Therefore, it would be incorrect to consider the contracts as involving unlawful activity. As these laws themselves recognize, they do not apply to contracts like Kalshi's.

A key purpose of the CEA and granting the CFTC exclusive jurisdiction over futures was to authorize and promote trading of futures contracts notwithstanding state laws that might purport to prohibit them as gambling. The only way in which state law is relevant is if the activity underlying the event contract violates state law, such as a contract on murder or state income tax evasion.[34] In that case, Congress wanted to make sure that a futures contract would not legitimize that blatantly illegal activity without the Commission considering whether trading the contract would be contrary to the public interest.[35]

As for the federal prohibition on interstate betting, the Wire Act is irrelevant here–it applies only to sports betting and wagering. Moreover, when Congress most recently addressed the intersection of gambling/gaming and the Internet, it carved out derivatives contracts (both on exchange and over the counter) from the definition of betting and wagering, thereby plainly recognizing that derivatives contracts serve economic purposes that distinguish them from gambling/gaming.[36] Congress recognized this much earlier too, granting the CFTC exclusive jurisdiction over futures as noted above and expressly preempting state gaming laws in the CFMA.[37]

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to derivative products that are excluded or exempt from the CEA. *See* 7 USC 16(e)(2) ("This Act shall supersede and preempt the application of any State or local law that prohibits or regulates gaming or the operation of bucket shops . . . in the case of --- (A) an electronic trading facility excluded under section 2(e) of this Act; and (B) an agreement, contract, or transaction that is excluded from this Act under [provisions of] the Commodity Futures Modernization Act of 2000, or exempted under section 4(c) of this Act.").

[33] *Ibid*

[34] We note some commenters have compared these contracts as equivalent, hypothetically, to contracts on mass shootings. The analogy is clearly incorrect and is a gross misinterpretation of the statute.

[35] Congress obviously would not be concerned about legitimizing elections. Even if the focus comes to legitimizing the trading on elections as part of the ultimate public interest analysis, the Commission has already crossed that bridge by long permitting market participants to trade such contracts pursuant to no action letters awarded to unregulated markets. The notion that allowing a regulated exchange to offer the contracts is what changes the public interest analysis is insupportable.

[36] The Unlawful Internet Gambling Enforcement Act of 2006 "do[es] not include…any transaction conducted on or subject to the rules of a registered entity or exempt board of trade under the Commodity Exchange Act". 31 U.S.C. § 5362(1)(E) (2006).

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Additionally, many broad state gambling laws would define all event contracts as gaming, as well as many other futures, swaps, and options. States like New Hampshire, for example, define gambling as having "to risk something of value upon a future contingent event not under one's control or influence."[38] If the Commission were to find that the contracts involve unlawful activity on the theory that there are state laws (or a federal law) prohibiting gambling/wagering on elections, and that wagering is equivalent to taking a position on an event contract, that would mean that the Special Rule is triggered by *any* event contract because many state gambling laws prohibit wagering on the outcome of *any* future event. That interpretation was clearly not Congress' intent. Instead, Congress narrowly defined a small number of event contracts whose underlying event involves an unsavory activity that Congress did not want the CFTC to legitimize without evaluating whether trading a contract on that activity would be contrary to the public interest (as per the text, which isolates a selected set of enumerated events to target).

Time and time again, Congress and states have indicated that the Commission has the decision making power here and approval of Kalshi's contracts has no involvement with unlawful activity any more than an event contract on Gross Domestic Product or whether a bill becomes law. If the Commission chooses to isolate these contracts as involving unlawful activity but not those many others, it would be acting contrary to Commission precedent and in an arbitrary way.

5. In determining whether these contracts involve an activity that is unlawful under any State or Federal law, should the Commission be influenced by whether state laws permit betting on the outcome of elections or other political outcomes and/or by the prohibition of interstate betting under Federal law?

No. The contracts solely involve the partisan affiliation of the Speaker of the U.S. House of Representatives and the President *pro tempore* of the U.S. Senate.

This issue was addressed in the previous question's response. It has been copied here for ease. The contracts also do not involve unlawful activity because of state prohibitions against election

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to derivative products that are excluded or exempt from the CEA. *See* 7 USC 16(e)(2) ("This Act shall supersede and preempt the application of any State or local law that prohibits or regulates gaming or the operation of bucket shops . . . in the case of --- (A) an electronic trading facility excluded under section 2(e) of this Act; and (B) an agreement, contract, or transaction that is excluded from this Act under [provisions of] the Commodity Futures Modernization Act of 2000, or exempted under section 4(c) of this Act.").

[38] New Hampshire Rev Stat § 647:2(II)(d) (2017); see also Alaska Stat. § 11.66.280(3) ("gambling" means that a person stakes or risks something of value upon the outcome of a contest of chance or a future contingent event not under the person's control or influence, upon an agreement or understanding that that person or someone else will receive something of value in the event of a certain outcome"); Oregon Rev. Stat. § 167.117(7) ("'Gambling' means that a person stakes or risks
something of value upon the outcome of a contests of chance or a future contingent event not under the control or influence of the person . . .").

'wagering' or 'betting', or federal laws prohibiting interstate 'betting'. Two arguments below explain why.

First, because per the Special Rule, only the underlying event (Congressional control) should be considered in determining whether the contracts involve gaming. The application of the Special Rule with regards to this question is addressed at length in a separate comment, which also includes letters provided by our counsel, former CFTC General Counsels Jonathan Marcus and Dan Davis.[39] Additional commenters on the matter include former MPD Director Josh Sterling, our director Timothy McDermott, as well as other public comments by former CFTC officials and industry actors such as Daniel Gorfine, Lewis Cohen, Tabet DiVito & Rothstein, and Jeremy Weinstein.[40]

Second, taking a position in an event contract is not equivalent to, as states or the federal government may define it, 'wagering' or 'betting' which they prohibit. This is not true legally (interstate betting is illegal, and betting is illegal in many states; event contracts are legal in all jurisdictions) or in practice. As "father of futures" Dr. Richard Sandor wrote in his comment letter,

> A major misconception that still prevails among the public is the equivalence of gambling and speculation. Nothing could be farther from the truth. Gambling is an artificial, self-constructed risk created for recreation. Speculation is the assumption of risks that already exist in the real and financial markets. The recreational risk of gambling is not present until the casino or racetrack is built and wagers are accepted. On the other hand, risk in the production of good and services in the economy are real and will exist even in the absence of futures markets. The same can be said for equity and interest rate and risk. It seems reasonable to conclude the risks associated with policy changes from different election outcomes are most similar to the latter. The transfer of risk by hedgers would be real and the assumption of that risk by speculators would be proper.[41]

Taking a position in an event contract is also not equivalent to the unlawful activity such laws refer to, because such laws are not operative on CFTC-regulated products. Federal law definitions of gaming, betting, wagering carve out exemptions for CFTC-regulated products.[42] Many states' gaming provisions also include such exemptions.[43] States' gaming provisions are

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[39] Public comment by Elie Mishory. Available at https://comments.cftc.gov/PublicComments/ViewComment.aspx?id=70781.
[40] Public comments 69737, 69687, 70755, 69736, 70765, and 69723.
[41] Public comment by Richard Sandor. Available at https://comments.cftc.gov/PublicComments/ViewComment.aspx?id=70792.
[42] The Unlawful Internet Gambling Enforcement Act of 2006 "do[es] not include…any transaction conducted on or subject to the rules of a registered entity or exempt board of trade under the Commodity Exchange Act". 31 U.S.C. § 5362(1)(E) (2006).
[43] For example, Washington state RCW 21.30.030 clarifies that CFTC-regulated transactions are not affected by its anti-bucket shop provisions.

preempted explicitly as well by the CFMA.[44] Even derivatives products that are excluded or exempted from CFTC regulation still preempt state gaming and bucket shop laws per the CFMA.[45] It could not follow more plainly that CFTC-regulated derivatives have the same preemptive effect. Congress has repeatedly recognized that futures and other derivative contracts serve economic purposes and, therefore, state laws that purport to prohibit or regulate futures or derivative contracts (including gaming laws) do not violate the CEA and are preempted. All of this shows that Congress and the states understand that there is a critical distinction between betting and legitimate financial activity. Election contracts that are designed for hedging on a financial market constitute legitimate financial activity. Therefore, it would be incorrect to consider the contracts as involving unlawful activity. As these laws themselves recognize, they do not apply to contracts like Kalshi's.

A key purpose of the CEA and granting the CFTC exclusive jurisdiction over futures was to authorize and promote trading of futures contracts notwithstanding state laws that might purport to prohibit them as gambling. The only way in which state law is relevant is if the activity underlying the event contract violates state law, such as a contract on murder or state income tax evasion. In that case, Congress wanted to make sure that a futures contract would not legitimize that activity without the Commission considering whether trading the contract would be contrary to the public interest.[46]

As for the federal prohibition on interstate betting, the Wire Act is irrelevant here–it applies only to sports betting and wagering. Moreover, when Congress most recently addressed the intersection of gambling/gaming and the Internet, it carved out derivatives contracts (both on exchange and over the counter) from the definition of betting and wagering, thereby plainly recognizing that derivatives contracts serve economic purposes that distinguish them from gambling/gaming.[47] Congress recognized this much earlier too, granting the CFTC exclusive

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[44] 7 USC 2(a)(1) covers exclusive CFTC jurisdiction over futures and swaps, so any state laws that would purport to regulate or prohibit futures or swaps would be preempted.. The CEA also preempts state gaming laws with respect to derivative products that are excluded or exempt from the CEA. *See* 7 USC 16(e)(2) ("This Act shall supersede and preempt the application of any State or local law that prohibits or regulates gaming or the operation of bucket shops . . . in the case of --- (A) an electronic trading facility excluded under section 2(e) of this Act; and (B) an agreement, contract, or transaction that is excluded from this Act under [provisions of] the Commodity Futures Modernization Act of 2000, or exempted under section 4(c) of this Act.").

[45] *Ibid*

[46] Congress obviously would not be concerned about legitimizing elections. Even if the focus comes to legitimizing the trading on elections as part of the ultimate public interest analysis, the Commission has already crossed that bridge by long permitting market participants to trade such contracts pursuant to no action letters awarded to unregulated markets. The notion that allowing a regulated exchange to offer the contracts is what changes the public interest analysis is insupportable.

[47] The Unlawful Internet Gambling Enforcement Act of 2006 "do[es] not include…any transaction conducted on or subject to the rules of a registered entity or exempt board of trade under the Commodity Exchange Act". 31 U.S.C. § 5362(1)(E) (2006).

jurisdiction over futures as noted above and expressly preempting state gaming laws in the CFMA.[48]

Additionally, many broad state gambling laws would define all event contracts as gaming, as well as many other futures, swaps, and options. States like New Hampshire, for example, define gambling as having "to risk something of value upon a future contingent event not under one's control or influence."[49] If the Commission were to find that the contract involve unlawful activity on the theory that there are state laws (or a federal law) prohibiting gambling/wagering on elections, and that wagering is equivalent to taking a position on an event contract, that would mean that the Special Rule is triggered by *any* event contract because many state gambling laws prohibit wagering on the outcome of *any* future event. That interpretation was clearly not Congress' intent. Instead, Congress narrowly defined a small number of event contracts whose underlying event involves an unsavory activity that Congress did not want the CFTC to legitimize without evaluating whether trading a contract on that activity would be contrary to the public interest (as per the text, which isolates a selected set of enumerated events to target).

Time and time again, Congress and states have indicated that the Commission has the decision making power here and approval of Kalshi's contract has no involvement with unlawful activity any more than an event contract on Gross Domestic Product or whether a bill becomes law. If the Commission chooses to isolate these contracts as involving unlawful activity but not those many others, it would be acting contrary to Commission precedent and in an arbitrary way.

6. Are the contracts substantively different from Nadex's previously proposed political event contracts such that the Commission's analysis should be different? For reference, please see "CFTC Order Prohibiting North American Derivatives Exchange's Political Event Derivatives Contracts" (Apr. 2, 2012), available at https://www.cftc.gov/PressRoom/PressReleases/6224-12.

There are a number of important distinctions between these Contracts and the Nadex contracts: (i) the contemporary understanding of the contracts' value, economic and otherwise, is more

[48] 7 USC 2(a)(1) covers exclusive CFTC jurisdiction over futures and swaps, so any state laws that would purport to regulate or prohibit futures or swaps would be preempted.. The CEA also preempts state gaming laws with respect to derivative products that are excluded or exempt from the CEA. *See* 7 USC 16(e)(2) ("This Act shall supersede and preempt the application of any State or local law that prohibits or regulates gaming or the operation of bucket shops . . . in the case of --- (A) an electronic trading facility excluded under section 2(e) of this Act; and (B) an agreement, contract, or transaction that is excluded from this Act under [provisions of] the Commodity Futures Modernization Act of 2000, or exempted under section 4(c) of this Act.").

[49] New Hampshire Rev Stat § 647:2(II)(d) (2017); see also Alaska Stat. § 11.66.280(3) ("gambling" means that a person stakes or risks something of value upon the outcome of a contest of chance or a future contingent event not under the person's control or influence, upon an agreement or understanding that that person or someone else will receive something of value in the event of a certain outcome"); Oregon Rev. Stat. § 167.117(7) ("'Gambling' means that a person stakes or risks
something of value upon the outcome of a contests of chance or a future contingent event not under the control or influence of the person . . .").

robust, (ii) there is data available to the Commission today that was not available to it in 2012 to assist its assessment of the Contracts' economic purpose and hedging utility. It was for these reasons that Mark Wetjen, former Commissioner and Acting Chairman and who served when the agency ruled against Nadex, supports Kalshi's submission.[50]

First, the understanding of the scope and significance of how market participants face risk from elections and attempt to hedge and manage their risks is much greater today than it was when the Commission considered Nadex's contracts. Today, news articles frequently discuss election risk and limited hedging opportunities.[51] Studies and commenters have discussed how banks engage in such hedging, both using traditional instruments and over-the-counter products.[52] In recent years, CEOs use the word 'election' at very high rates on earnings calls near election time.[53] Additionally, there is now data on the correlation between perceived election outcomes and pricing of financial assets that were not available when the Commission considered Nadex. Many researchers utilized data from PredictIt to study the link between market based election outcome pricing, along with election polling and the impact on pricing financial assets.[54] They also consistently found that it was often more dynamic and accurate than polling.[55] These findings by academics have been replicated many times, as described in Kalshi's original submission at length.

Second, the understanding of the public interest factors of the contracts is very different today than it was when the Commission considered the Nadex contracts. Victoria University of Wellington's operation of its exchange pursuant to a CFTC no-action letter provided evidence and data from trading on these markets and other similar markets (including more local markets) over a period of close to eight years. PredictIt has traded more than a billion shares.[56] Its markets were consistently referenced, in real time and in hindsight, as informative and useful by major news organizations like *CNN*, *CNBC*, *Politico*, *Bloomberg*, *The Economist*, *The Wall Street Journal*, *The Washington Post*, and across various sections of *The New York Times* like *The*

[50] Public comment by Mark Wetjen. Available at https://comments.cftc.gov/PublicComments/ViewComment.aspx?id=70771.
[51] There are too many examples to cite. Some can be found at Refinitiv ("A US Election Hedge"), Barron's ("This Election Could Be Really Weird. Hedge Your Portfolio"), or Yahoo Finance ("How To Hedge Your Portfolio For The Election"), all from the last 5 years. Available at: https://www.refinitiv.com/en/the-big-conversation/episode-48-a-us-election-hedge, https://www.barrons.com/articles/this-election-could-be-really-weird-hedge-your-portfolio-51599130801, and https://finance.yahoo.com/news/hedge-portfolio-election-173325198.html.
[52] Public comment by Angelo Lisboa. Available at https://comments.cftc.gov/PublicComments/ViewComment.aspx?id=69666.
[53] John Butters. 2020. "More than one third of S&P 500 companies are discussing the election on Q3 earnings calls." Factset.
[54] Such as Snowberg, Zitzewitz, and Wolfers (2006); Zitzewitz and Wolfers (2016); and Jayachandran (2016). Available at: https://www.frbsf.org/economic-research/publications/working-papers/2006/08/, https://www.brookings.edu/research/what-do-financial-markets-think-of-the-2016-election/, and https://escholarship.org/content/qt25p4z52g/qt25p4z52g.pdf?t=krnmet.
[55] Miller, Thomas W. "Predicting the 2020 Presidential Election." *Data Science Quarterly*. 2021.
[56] LinkedIn profile of Will Jennings, former PredictIt employee. https://www.linkedin.com/in/will-jennings-pi

Upshot, *DealBook*, opinion columns, and the technology section. The reliance on PredictIt demonstrates the public's interest and social value in its data across all spectrums of society. In addition, information generated from PredictIt's markets was repeatedly cited by prominent political officials and commentators. Examples include economists like Jason Furman, previously President Obama's Council of Economic Advisors Chair (who submitted a supportive comment letter which noted PredictIt's election market data was used while he was in the White House); Nobel Laureate Paul Krugman, a Professor at Graduate Center, CUNY and a columnist for *The New York Times*; and data scientists/reporters like Nate Silver, founder and editor-in-chief of *FiveThirtyEight*.[5758] All of this strong support for the contract's public interest was not available to the Commission when it considered Nadex.

Additionally, the fears driving the *Nadex Order* with respect to election integrity–that voters could be incentivized to switch votes given election markets–has never been realized or suggested. The complete lack of evidence for the concern in the *Nadex Order*, despite a massive growth in election trading post-*Nadex*, is highly probative. PredictIt traded over 1.2 billion shares from 2014 to the present.[59] U.S. elections traded around $250 million between off-shore exchanges like InTrade and BetFair in 2012; by 2020, PredictIt and Betfair alone combined for nearly $1b in trading.[60] The Commission's fear, speculative at the time, has been rebutted through recent history with materially similar market activity. For these reasons, the Commission's past – and speculative – concern that approving the Nadex contracts would create monetary incentives to vote for a particular candidate cannot be relied on again.

Finally, these markets have grown dramatically despite the *Nadex Order*. The public is very interested in the information provided by these markets, even when that information comes from unregulated or offshore sources. While market demand for a product is not sufficient alone to determine the public interest, it is undeniably an important factor that the Commission should consider in determining whether a contract is contrary to that interest. It is unlikely that the Commission would disagree that its many Core Principles and regulatory oversight lead to a safer market experience for participants. Accordingly, there is significant public interest in having these markets available on regulated exchanges.

Similarly, especially with regard to Congressional control contracts, it is important that market activity not be a detrimental or negative force. There are obvious benefits to market activity occurring under the sanitizing light of regulation–as Justice Louis Brandeis said, "sunlight is said

[57] Public comment letter by Jason Furman. Available at: https://comments.cftc.gov/PublicComments/ViewComment.aspx?id=69708.
[58] For the sake of brevity, a full list of citations in this section can be found at the end of this document.
[59] LinkedIn profile of Will Jennings, former PredictIt employee. https://www.linkedin.com/in/will-jennings-pi
[60] Full breakdown of volume at end of document.

to be the best disinfectants."[61] The demonstrated rapid growth of this activity is unlikely to abate absent significant actions from the Commission to *prevent* the activity, a tall task given constrained Commission resources, the breadth of these markets, and the ease of their creation. Accordingly, these markets will likely continue to exist. The question is whether they will exist also in a regulated market or remain just in the unregulated shadow market. This is of course not a reason to permit the contracts *independently* of the Contract's economic utility. But it is an undeniably important public interest consideration. Because the breadth of the current unregulated marketplace is a more recent development, this public interest consideration was not before the Commission when it considered Nadex.

The Exchange also notes that exchanges are not granted exclusive licenses to list products. If the Commission would allow these contracts, Nadex would generally be able to list the same contracts Kalshi is proposing today.

7. Are the contracts substantively different from Kalshi's previously proposed, and withdrawn, congressional control contracts? For reference, please see "CFTC Announces Review and Comment Period of KalshiEX Proposed Congressional Control Contracts Under CFTC Regulation 40.11" (August 26, 2022), available at https://www.cftc.gov/PressRoom/PressReleases/8578-22.

Kalshi's contract was modified in response to Commission questions, the public comments, and Commission staff feedback. There are three changes to the contract:

1. An increase in the position limits from $25,000 for all participants to a tiered system for retail, institutions, and eligible contract participants that allows for potentially much higher limits.
2. An increase in the order size to 5000 contracts, from 1.
3. A list of political actors who are prohibited from trading were detailed.

Whether the proposed contract is "substantively different" is a semantic matter. The contract serves broadly the same economic purpose but has been more narrowly tailored to promote *bona fide* hedging behavior and gate out potential insiders. In practice, the contract will be used less by smaller retail users compared to the previous submission. Kalshi's previous submission is still compliant with the Core Principles and the Act, and would serve the public interest by virtue of its hedging, price basing, and forecasting benefits.

What is clear and obvious is that this contract that is before the Commission, like the prior contract, can be used to hedge risk exposure to political control, and will serve as a price

[61] Brandeis, Louis. "What Publicity Can Do." 1914. Accessed via the website of the Louis D. Brandeis School of Law Library. Available at https://louisville.edu/law/library/special-collections/the-louis-d.-brandeis-collection/other-peoples-money-chapter-v

discovery tool for the market's pricing of the likelihood of the various outcomes of political control.

Further, just as the Special Rule for Event Contracts does not apply to the prior contract because the underlying event is not one of the enumerated events, so too it does not apply to this contract.

8. Do the contracts serve a hedging function? What standard should be used in reviewing the contracts' hedging function? Is it sufficient that a contract could theoretically be used for hedging, or should an exchange provide evidence of demonstrated need by likely hedgers in the market? How often must a contract be used for hedging or what percentage of market participants or open interest must represent hedging use in order for a contract to serve a hedging function?

Yes, the contracts serve a hedging function. The financial press frequently reports on how elections (and changes in election polling, no less) affect the prices of financial assets, well before any laws by the new Congress have been enacted.[626364] Academic research consistently finds a link between movements in election prediction markets and financial assets, as well as between polls and financial assets.[65] Even though the exact consequences of elections are not certain, political parties make sufficiently credible commitments to changing government policies in a manner that market participants currently believe are predictable enough–they're already pricing in the risk and putting money on the line.

The remaining elements of the question can be unpacked as follows:

1. An assumption that the Commission should review a contract's hedging function.
2. Should the standard for hedging be theoretical use or demonstrated need?
    a. Must a contract's participants have a minimum required amount of hedging (either in absolute or percentage terms)?

The Exchange will address these seriatim. However, the Exchange notes that regardless of the standard, the contracts here passes: *Kalshi has demonstrated hedging need.* In its submission to DMO in March 2022, Kalshi provided many examples of consistent evidence of ongoing hedging in the public and private markets via testimony from market participants and academia. Many retail investors, small businesses, billion-dollar businesses, and members of industry provided comments testifying to their personal hedging use cases. These included those by Alex

[62] Noel Randewich. 2020. "S&P 500 futures rise as U.S. election suggests less regulatory risk." Reuters.
[63] Myra P. Saefong. 2020. "Here's how the U.S. presidential election could shake up the oil market." Marketwatch.
[64] Matthew Weaver. 2020. "Congressional elections could impact commodity prices most, expert says." *Capital Press*.
[65] Such as Snowberg, Zitzewitz, and Wolfers (2006); Zitzewitz and Wolfers (2016); and Jayachandran (2016). Available at: https://www.frbsf.org/economic-research/publications/working-papers/2006/08/, https://www.brookings.edu/research/what-do-financial-markets-think-of-the-2016-election/, https://escholarship.org/content/qt25p4z52g/qt25p4z52g.pdf?t=krnmet.

Keeney, Ali Partovi, Arvind S, Jun Sup Lee, Edward Makino, Ramin Ahmari, Valentin Perez, Donald Stalter, Alexander King, Kenn Butler, Vivek Ranadive, Thomas Dalton Combs, among so many others.[66]

There is nothing more Kalshi and potential hedgers could have done in order to demonstrate the hedging need this product fills.

1: Should the Commission review a contract's hedging function?

There is no requirement from Congress, nor mechanism by which, the Commission can or should determine hedging utility as a metric on its own outside of the public interest. However, a contract's hedging utility can be considered as supporting the public interest as part of the public interest consideration should the Commission find that a contract involves one of the enumerated activities of the Special Rule.

2: What standard should the Commission use, theoretical use or demonstrated need?

A contract's hedging utility may be an important consideration in favor of finding that a contract is not contrary to the public interest should the Commission find that it involves one of the enumerated activities of the Special Rule. Hedging is in the public interest and promoting risk mitigation is a core mission of the CFTC. The Exchange notes, however, that these two suggestions ('theoretical' versus 'demonstrated need') are more like opposite ends of a spectrum, and there are variations in between.

It should use a theoretical use standard. A demonstrated need standard could inhibit the creation of new products with smaller or less clear markets; has no clear mechanism by which it can be determined; and because a contract only theoretically being used for hedging is not contrary to the public interest.

It should not be missed that the standard implied in the last part of this question (some minimum required amount of hedging, in absolute or percentage terms) would be likely to have unintended consequences if imposed on the market.

1. This standard has not been imposed on *any other contract in Commission history*, including any event contract. There are only 90 million barrels of oil produced per day, but almost 1 billion barrels are traded on Chicago Mercantile Exchange's crude oil futures every day (not to mention other highly traded products, like Intercontinental Exchange's West Texas Intermediate or Brent contracts).[67] The overwhelming majority of

[66] See comments 69612, 69608, 69671, 69647, 69696, 69669, 69725, 70770, 69709, 70776, 70757, 70767.
[67] CME Crude Oil Futures Volume & Open Interest. Available at https://www.cmegroup.com/markets/energy/crude-oil/light-sweet-crude.volume.html.

activity is not primary hedgers. Nonetheless, the market has clearly added value to the global financial system.

2. The percentage of the Contract's participants hedging will no doubt vary over time in a vibrant, dynamic marketplace as risks change.
3. Speculation is an accepted important use case for all contracts in the financial markets. Speculation on events of economic purpose is not equivalent to gaming or gambling, and has never been considered that. Non-hedgers help balance out any differences between short and long hedgers, and provide liquidity to the hedgers themselves. Without speculation, none of the major futures and derivatives markets would be as liquid as they are today, and thus as powerful in fulfilling the hedging utility as they are. Speculation improves a contract's hedging utility. Even in cases where the non-hedgers are not actually matching on the exchange with the hedgers, they are providing a valuable service to the hedgers. The price offered on an exchange is a function of many factors, including demand and liquidity–non-hedgers will demand a greater premium if they know it will be harder for them to exit their positions later if their needs change. So the presence of later non-hedgers willing to provide liquidity and trading volume is essential to encouraging the original round of liquidity providers to offer more competitive prices to the hedgers, since the original liquidity providers know that they will not have an issue exiting their positions later. As Commissioner Quintenz put it:

> Whereas bettors participate in games of pure chance, whose sole purpose is to completely reward the winner and punish the loser for an outcome that would otherwise provide no economic utility (think roulette), speculators in the derivatives market participate in non-chance driven outcomes that have price forming impacts upon which legitimate businesses can hedge their activities and cash flows… The other factor which makes speculation different than pure-chance gambling is the price forming impact it has on markets which allow businesses to hedge their risk.[68]

9. Are there unique economic risks tied to the outcome of congressional control that cannot be hedged via derivative products on equities, debt, interest rates, tax rates, asset values, and other commodity prices?

The Commission's question can be taken to imply two different things, either that the other products are linked directly on the same risks that the contracts would be used for hedging, or that market participants can reasonably approximate the Contract's hedging utility via a melange of other instruments.

Assuming the former, the answer is yes, there are risks that cannot be currently hedged. First, as noted by Hehmeyer and other commenters, and in the Exchange's submission, there are significant direct, non-policy related economic risks, such as the risks imposed by political

[68] Quintenz, *ErisX*.

outcomes on the fortunes of media personalities, media consultants, and others with connections and ties to the party in power. These risks cannot be otherwise hedged by traditional products.

As discussed earlier, changes in general risk that a certain Congress could pose to various industries can be discerned well in advance of knowledge of the particular policies that may be implemented by that Congress and provide just as valid a hedging rationale. This difference results from the time horizon between the election cycle and the implementation of a new Congress' specific legislative agenda or its potential responses to current events. For example, following the election of Republicans into Congress in 2016, many publications speculated that trade policy would become more restrictive; however, it was not known if this would come in the form of new trade deals, re-negotiating existing trade agreements, new tarrifs (and if so, on what goods and at what level), international lawsuits, and more. Another event contract or future on taxes or public policy would not have been very helpful. However, the risk of a more restrictive policy was there because of who would win the election, exactly what Kalshi's contracts allow traders to hedge.

Another example is new legislation that would burden a market participant. Once the legislation draft is released, the impact will begin to be felt immediately (on assets, cash flows, and partnerships as market participants price in risk), making a hedge useless; the downside risk has already had much of its effect. Markets are forward looking, and hedging products should reflect that. Even just a statement by a politician can be very damaging for firms.[69]

Additionally, a single market participant may face myriad risks from elections. Many firms and individuals are negatively affected by a suite of a party's policies, and thus wish to hedge the many different changes in risk through a single contract. For example, an oil company may wish to hedge the risk that a new Democratic government will come into office, because that government could not only impose new regulations on them but also change the composition of existing regulatory bodies and increase their labor costs (through raising the minimum wage, supporting unionization, or mandating greater health care benefits for employees). Only Kalshi's proposal lets them hedge the risk they actually face: Democratic government.

If the question is asking instead whether market participants can reasonably approximate the Contract's hedging utility via a melange of other instruments, the answer is they cannot. Many retail and small business market participants do not have access to these other instruments, and the inherent friction and transaction costs in arranging these types of complex proxy plays is prohibitive. It seems unlikely that the Commission would determine it in the public interest to solely rely on these tools that are inaccessible to many of the market participants who need risk management tools most. Additionally, the effectiveness of these baskets and combination of

[69] White, Spencer. "Hillary Clinton Blog Post Hits Valeant Stock For 9% Loss Without Revealing New Policy." Yahoo Finance. 2016.

instruments to hedge the risk from political control is considerably less than a contract directly on political control.

Importantly, the question implies that its answer matters, but does not explain why it would. A reasonable inference is that the Commission is saying no new method of hedging a risk should be permitted if there are other existing methods of hedging that risk. Nowhere in the CEA or the Commission's Regulations is there such a standard. The Exchange hopes this is not the Commission's view, as it has not been the Exchange's experience when engaging with the Commission on prior contracts. For example, should the Commission say "farmers can buy crop insurance therefore they should not have access to agricultural futures products"?

Furthermore, such an interpretation would be highly anti-competitive. Such an interpretation would mean that if one firm offers a contract on an event or a commodity, that no challenger should enter the market with a similar but different product to compete with it. In fact, such an interpretation would consistently punish novel or innovative products – in many cases, it is possible to construct a hedge using existing products, and attempting to do so might be expensive or incur excess basis risk. The fact that election risk has implications for other assets is, in fact, much of the justification *for* the contract's hedging utility and would work in concert with such assets. Many similar and competing products are listed by different exchanges in order to promote a vibrant and competitive marketplace for hedgers. This is also an important component of the contract's price discovery utility, discussed in a later question.

Such an interpretation would also curtail innovation. Innovation often happens through iterating on already successful products and ideas. As in the earlier example, the existence of insurance products would have inhibited the creation of futures. Innovation often requires creating new, and sometimes flawed, products in order to try and optimize use cases for market participants. Hedgers benefit when many exchanges are launching many different products to try and tailor to their needs; they suffer when the government limits their options. It's in the public interest for such innovation to occur, and for that to happen, the Commission should not take the view that this product should not be listed because it purportedly can be hedged through other means.

10. Are the economic consequences of congressional control predictable enough for a contract based on that control to serve a hedging function? Please provide tangible examples of commercial activity that can be hedged directly by the contracts or economic analysis that demonstrates the hedging utility of the contracts.

Yes. The financial press frequently reports on how elections (and changes in election polling, no less) affect the prices of financial assets, well before any laws by the new Congress have been

enacted.[707172] Academic research consistently finds a link between movements in election prediction markets and financial assets, as well as between polls and financial assets.[73] Even though the exact consequences of elections are not certain, political parties make sufficiently credible commitments to changing government policies in a manner that market participants currently believe are predictable enough–they're already pricing in the risk and putting money on the line.

Investment banks routinely provide clients with advice on hedging through their private wealth divisions. This was described in a comment letter provided by a Managing Director of JPMorgan Chase. He wrote,

> At JPMorgan, election risk is one of the largest risks our clients face, and they frequently engage us proactively on how to minimize it (hedge it, in other words). We work with and advise our clients on how to avoid that risk in their portfolios, especially when a client's cash flows or investments are very politically sensitive (for example, those in the coal industry are very concerned regarding election outcomes and policy expectations).
>
> Since clients have different risk profiles, we do extensive research to fine-tune how these risks add up in our clients' positions. Our division employs a team of economists, at service to our partners, whose role in election years is heavily to research election probabilities as well as the impact election outcomes will have on equities and other investment products. We frequently host discussions with experts and clients on the relevant risks (including one coming up this week!) and publish research for both clients and the public.[74]

Investment banks also publish research to money managers (and the public, as the above mentions) that provides advice on how to hedge election risk in very specific ways. For example, JP Morgan Chase projected that a Democratic victory in 2020 would lead to a rally in 'left-behind' equities, such as "European cyclicals, value, China-exposed stocks and renewables" and portfolios should be adjusted accordingly.[75]

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[70] Noel Randewich. 2020. "S&P 500 futures rise as U.S. election suggests less regulatory risk." Reuters.
[71] Myra P. Saefong. 2020. "Here's how the U.S. presidential election could shake up the oil market." Marketwatch.
[72] Matthew Weaver. 2020. "Congressional elections could impact commodity prices most, expert says." *Capital Press*.
[73] Such as Snowberg, Zitzewitz, and Wolfers (2006); Zitzewitz and Wolfers (2016); and Jayachandran (2016). Available at: https://www.frbsf.org/economic-research/publications/working-papers/2006/08/, https://www.brookings.edu/research/what-do-financial-markets-think-of-the-2016-election/, https://escholarship.org/content/qt25p4z52g/qt25p4z52g.pdf?t=krnmet.
[74] Public comment by Angelo Lisboa. Available at https://comments.cftc.gov/PublicComments/ViewComment.aspx?id=69666.
[75] Ksenia Galouchko. 2020. "JPMorgan Says Biden Victory Could Mark a Stock Market Shift." Bloomberg.

Many other comment letters by retail traders (Raphael Crawford-Marks, Scott Supak, Jacob Colbert, Jacob Faircloth, Andrew Karas, Joseph Turano, among many others), industry leaders (Jorge Paulo Lemann, Christopher Hehmeyer, Ron Conway, Seth Weinstein, among many others) and owners of politically sensitive businesses, (Continental Grain Company, Klarna, Greenwork, Upsolve, among many others) agreed and specifically discussed personal hedging use cases.[76] Consider the comment by Scott Supak:

> In the more immediate political future, the hedging benefits are obvious: since I'm no longer employed through my union, my wife no longer has health coverage through my union, so we must purchase (very expensive) health insurance from the marketplace. When it seems that Republicans are likely to take control, I can invest in that possibility, and hedge against the risk that her health insurance premiums will go up (or that the subsidy will get smaller, or that her ability to purchase insurance at all is taken away completely).[77]

Or the comment by Greg Sirotek, the co-founder and CEO of Moneytree Power, a startup dedicated to installing solar power:

> Congress has an incredible influence over the future of the zero-carbon energy industry, particularly the solar industry…Given the respective differences in the two parties' positions on the importance of climate change mitigation, renewable energy development and the deficit, the risk profiles depending on which party is in power is vast. An event contract which pays out on the basis of Congressional control would allow our business to manage this previously unhedged risk.[78]

Lemann, a founder at 3G Capital (one of the world's largest investment firms) and a Board member of firms like AB-InBev and Kraft Heinz (some of the largest participants in traditional agricultural and metals futures), wrote:

> These statements [the *Nadex Order*'s claims that there are no hedging or price basing use cases for elections] are inconsistent with the preponderance of the academic research on the subject and is inconsistent with the actual experience of anyone who has ever operated a business in or with the United States or traded on the global commodity markets. Experience and empirical observation show that elections have consequences,

[76] Public comments 69668, 69715, 69667, 69683, 69678, 69619, 69684, 69717, 69714, 69718, 69727, 69707, 69677, 69655.
[77] Public comment by Scott Supak. Available at https://comments.cftc.gov/PublicComments/ViewComment.aspx?id=69715
[78] Public comment by Greg Sirotek. Available at https://comments.cftc.gov/PublicComments/ViewComment.aspx?id=70751.

> and these consequences directly create risk that can be hedged, and are factored into pricing commodities, financial assets, and services.[79]

Hehmeyer, former Chair of the National Futures Association and Board Member of the Futures Industry Association, added that many are affected *regardless of policy outcomes*:

> For example, media personalities and companies face risk from Congressional control and elections. Early professionals hoping to work on Capitol Hill know there are far more positions available if their preferred party is victorious, as there are more Congressional offices and committee positions for them to staff. A consultancy that specializes in specific topic areas (for example, a green energy consultancy) may know the demand for their services will decline in anticipation that their issue of expertise is less likely to be operative under a split Congress. These risks occur regardless of the legislation that actually passes. There are billions of dollars at risk surrounding the outcome of Congressional control and elections. These risks can reasonably be expected to be managed through this contract on Congressional control.[80]

Although some commenters claimed election outcomes aren't predictable enough to be a useful hedge, that in no way contradicts or even diminishes those who say the opposite. *At most*, those commenters don't see hedging utility for themselves. But they cannot credibly say, especially given the comment file, that all the people who identify how they would use the contracts for hedging and managing their risk are mistaken or deficient in their ability to recognize risk and potential tools to manage or mitigate that risk. It would be arbitrary for the Commission to listen only to those who assert that there is no hedging use case for anyone when there are many others who state that they *would* use the product for themselves or their business.

As noted by Hehmeyer, there is sufficient impact from elections themselves, independent of the policy implications of political control, to not only justify these markets' economic utility but to make them valuable. In addition, markets already believe that the policy implications of elections themselves are sufficiently meaningful so as to be worth repricing assets, suggesting that they are predictable *enough*. Elections have vast consequences, which directly impact the likelihood of events happening or not happening (such as a bill being passed). While it is true that there is some uncertainty about the precise implementation of any given law by a new Congress (e.g., what exactly would the size of the stimulus checks be, what exactly would the new tax rate be), changes in probabilities are more than sufficient for hedging purposes. In addition, once the specifics of a policy risk have been announced (like the text of a bill), it's practically impossible to hedge because of the high cost now that the probability of the event has increased. It's

[79] Public comment by Jorge Paulo Lemann. Available at: https://comments.cftc.gov/PublicComments/ViewComment.aspx?id=69684.
[80] Public comment by Christopher Hehmeyer. Available at https://comments.cftc.gov/PublicComments/ViewComment.aspx?id=69717&SearchText=christopher.

important for a potential hedger to hedge in advance of the specifics of their risks being announced.

Changes in *general risk* also can provide a strong hedging need as opposed to the changes in risk of a specific outcome. If one party is in complete control of Congress, there is likely to be a change in *general* risk on carbon-based energy products and industries and an opposite change in *general* risk on renewable energy products and industries. While the specific policies implemented may be hard to know in advance, that change in *general* risk has been discussed at length in comment letters and is hedged extensively by larger institutions through complex products.[81]

Consider a concrete example of probabilistic change from the bond markets. Ten percent of the catastrophe bond market is in "parametric triggers," which means the bond pays out if certain meteorological triggers are met. The bond issuer does not know for certain whether the storm that meets the threshold will cause mass flooding, power outages and property damage (and conversely, it's possible that such damages could occur with a storm that does not meet the trigger thresholds) yet they use the bond to hedge nonetheless, because other features of the bond (hedging wind speed, namely) are more important to them than eliminating basis risk. Moreover, even if a wheat farmer buys a contract that pays out if the price of wheat falls below a certain threshold, there is still some uncertainty as to whether that event will harm them. It's possible that (a) wheat falls below a certain threshold because weather conditions are so great that there was a bumper crop and that the increase in their supply offset the loss in price, or (b) that the national price does not perfectly correlate with the local price they received–but they can use the product nevertheless.

11. Should the Commission consider contract and position sizes, size of trade requirements, and/or an exchange's intended customer base to help assess whether a contract is likely to be used for hedging in at least some cases? Does the requirement that all contracts listed on Kalshi must be fully-collateralized affect this analysis? Does the requirement that these contracts trade in multiples of 5000 and/or the position limits applicable to the contracts affect the analysis of the hedging utility of the contracts?

As noted earlier, outside of the public interest test, it is well settled that there is no required hedging test of the Contract, nor one provided by Congress, the rules, or the regulations.[82] Hedging should be an important consideration as part of a contract's public interest test should the Commission find that it involves one of the enumerated activities of the Special Rule, though

[81] Public comment by Angelo Lisboa. Available at https://comments.cftc.gov/PublicComments/ViewComment.aspx?id=69666.

[82] Even in the public interest test, the Exchange notes that it is not at all settled that the original "economic purpose test" was resurrected. The better reading is that Congress wanted the Commission to look at the variety of factors that are discussed in the CEA, its purpose, and the core principles.

it need not be the only consideration. Hedging is in the public interest and promoting risk mitigation is a core mission of the CFTC and Kalshi.

In addition, whatever standard the Commission uses, Kalshi's contracts are permissible. As evidenced by the public comments, the intended customer base is a mixture of hedgers, liquidity providers/market makers, forecasters, and speculators. This is consistent with the customer base of some of the world's largest commodity markets, and is thus wholly permissible. The Commission would be speculating to suggest otherwise given the large body of relevant evidence.

1: Should the Commission consider contract and position sizes, size of trade requirements, and/or an exchange's intended customer base to help assess whether a contract is likely to be used for hedging in at least some cases?

The Commission can consider factors beyond hedging utility in its public interest analysis, should it find that the contracts involve one of the enumerated activities of the Special Rule. However, it should not consider an exchange's intended customer base. This would be very speculative. Customer bases change over time. In many cases, an Exchange may use a product in order to attract a new customer base, so using past customers as the foundation for guessing what the "intended customer base" is would be erroneous. If anything, this test would inappropriately penalize any novel product, as those are the products most likely to have an intended customer base most different from the existing user base. In short, there is no basis in law for the Commission to speculate about whether an Exchange's "intended customer base" meets its standards.

Trade requirement sizes are also not relevant. It may affect the number of parties who use the contract, for what purpose, and in what capacity; but nonetheless, the contract cannot serve *less* of a hedging function because of the proposed trade size, which is neither exceptionally small nor large compared to derivatives products available on CFTC-regulated boards of trade.

2: Does the requirement that all contracts listed on Kalshi must be fully-collateralized affect this analysis?

Whether a contract is fully collateralized or margined should not influence the Commission's thinking. Further, in this case it would be irrelevant. The hedging use cases shown by the public comments and other evidence provided to the Commission by Kalshi show that there is no basis to conclude that full collateralization will deter or preclude hedging behavior. Individuals, small businesses, and medium-sized businesses are all interested in using the contracts as they stand and as Kalshi proposed. Accordingly, even if the Commission considered the full collateralization requirement, it would still easily pass the test.

There is one area where the full collateralization requirement becomes relevant and that is in regard to responsible innovation. As a foray into quasi-new territory, it makes sense that the Exchange has certified only a fully collateralized product. This requirement will prevent excessive leveraging, and while it certainly may be appropriate to have margin products on this in the future, as an initial product it is prudent and sensible to maintain Kalshi's requirement that the contract be fully collateralized. Indeed, Kalshi should be commended for its cautious approach to innovation.

3: Does the requirement that these contracts trade in multiples of 5000 and/or the position limits applicable to the contracts affect the analysis of the hedging utility of the contracts?

No. As discussed earlier, trade requirement sizes are not relevant. It may affect the number of parties who use the contract, for what purpose, and in what capacity; but nonetheless, the contract cannot serve *less* of a hedging function because of the proposed trade size, which is neither exceptionally small nor large compared to derivatives products available on CFTC-regulated boards of trade.

12. Should the Commission consider the contract design and payout to help assess the hedging utility of the contract? For example, are binary contracts useful for hedging nonbinary economic events?

1: Should the Commission consider the contract design and payout when trying to assess the economic utility of the contract?

As noted in previous responses, outside of the public interest test, there is no required hedging test of the Contract, nor one provided by Congress, the rules, or the regulations. Hedging may be an important consideration as part of a contract's public interest test should the Commission find that it involves one of the enumerated activities of the Special Rule, though it need not be its only consideration as part of that test. Hedging is in the public interest and promoting risk mitigation is a core mission of the CFTC.

In addition, as argued above, the Commission should not speculate about the exact amount or percentage of total trading that will be used to hedge. Instead, it should consider whether there are hedging use cases. It is not contrary to the public interest for the contracts to be utilized for hedging as often as the market sees fit to hedge–many contracts listed by other exchanges are traded very little at all.

In fact, it is in the public's interest for *the market* to determine whether or not a contract design is appropriate for hedging, not the Commission. If the contract design is a poor fit for hedging

needs–which it does not appear to be, especially given the many public comments by retail, small businesses, and industry in support–then Kalshi will attract fewer participants and in the future will amend the contract structure to improve. The incentives of the Exchange and hedgers are aligned. Substituting the Commission's judgment for the market's would short-circuit that valuable process. Accordingly, the Commission's inquiry into hedging as part of its public interest inquiry should be whether the contracts can be used for hedging. As noted, however, the contracts here have significant hedging utility that would pass any of these tests.

Moreover, different firms have different hedging needs, and different structures can best meet those needs. What works for one firm may not work best for another firm. As a result, the Commission should not attempt to speculate about whether a particular structure would work, as they may miss many firms for whom an alternative structure is better. The utility of the market is that there exists a profit incentive to create products for even niche groups of buyers, and insofar as private firms are far closer to their potential customer base than a government agency which does not interact with them on a daily basis (unlike an exchange), it would be highly inappropriate for the Commission to impose its judgment about whether a product's structure meets potential customer's needs. It's in the public interest to permit innovative contracts that they may use.

2: Are binary contracts useful for hedging nonbinary economic events?

On a superficial level, Congressional control is one of the most true "binary" events in the world: either the Republicans win or the Democrats win. While the margin in each chamber certainly matters (a 53-Democrat Senate does look different from a 50-Democrat Senate), there is a sharp, binary, discontinuity in economic effects when control tips from one party to another.

Perhaps the Commission might argue that while Congressional control is binary, the effects of Congressional control are non-binary. Some people (like energy firms) might be affected a lot, whereas other people (like an IT consultancy) might be affected relatively less. Then there exists a continuum between the energy firm and the IT consultant of people affected. However, it does not follow that binary events cannot be a suitable tool for hedging since the effects are still caused by the binary control.

But more importantly, binary products are still capable of hedging non-binary events. The Commission has allowed binaries on the federal funds rate on the Chicago Board of Trade, even though it is self-evidently true that some people are hurt (or helped) by changes in interest rates more than others.[83] The Commission has allowed event binaries on monthly inflation prints, even though the Consumer Price Index is a continuous distribution of real numbers. Hundreds of millions of dollars are traded annually on binary parametric trigger catastrophe bonds, even

[83] Hunt, Katherine. "CBOT to launch binary options on target federal funds rate." *MarketWatch*. 2006.

though the economic effects of such catastrophes are far from binary. And traders hedge probabilities, not absolutes. Accordingly, binary products are perfectly compatible as a hedging device with non-binary economic events.

13. Do the contracts serve a price-basing function? For example, could they form the basis of pricing a commercial transaction in a physical commodity, financial asset, or service?

Yes. As discussed earlier, the market frequently reprices assets on the basis of changes in election expectations and election outcomes.[848586] Evidence abounds from the market, the financial press, and academia.

In 2012, more than two dozen economists signed a letter to the Commission supporting Nadex's submission that argued as much. Led by the late Nobel Laureate Kenneth Arrow in that 2012 letter, they wrote:

> Political event futures facilitate price discovery in other asset markets. One of the findings of [our] research is that firms and industries are exposed to political and policy risk. Political event futures provide investors with a market-based assessment of outcome probabilities, which reduces investors' uncertainty when trading other assets.[87]

Many economists have done the same for Kalshi, including Nobel Laureate Robert J. Shiller, Phillip Tetlock, Justin Wolfers, Scott Sumner, Michael Abramowicz, Joseph Grundfest, Alex Tabarrok, Michael Gibbs, Jason Furman, David Pennock, Harry Crane, David Rothschild, Koleman Strumpf, Ryan Oprea, and others.[88] A letter signed by Pennock, Crane, Rothschild, and Strumpf argued,

> Prediction market prices in political and policy events would help facilitate price discovery in a wide-range of asset markets, affecting the entire economy (note that pricing is freely available to non-traders). Political and policy events matter: they expose a wide-variety of businesses to risk that traditional financial markets have trouble pricing. A robust set of markets for political and policy events could price that risk, and, if they were allowed to flourish, could eventually grow to provide hedges where uncertainty is particularly acute.[89]

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[84] Noel Randewich. 2020. "S&P 500 futures rise as U.S. election suggests less regulatory risk." Reuters.
[85] Myra P. Saefong. 2020. "Here's how the U.S. presidential election could shake up the oil market." Marketwatch.
[86] Matthew Weaver. 2020. "Congressional elections could impact commodity prices most, expert says." *Capital Press*.
[87] *Nadex* public comment by Zitzewitz et al. Available at https://www.cftc.gov/sites/default/files/stellent/groups/public/@rulesandproducts/documents/ifdocs/ericzitzewitzltr020312.pdf.
[88] See public comments 70761, 69708, and 69735.
[89] Public comment by David Rothschild. Available at https://comments.cftc.gov/PublicComments/ViewComment.aspx?id=69735.

The contracts can obviously be used to price MIAX's corporate tax futures and Kalshi's other political event markets related to bills passing, government shutdowns, and the debt ceiling. They can also be used to price other non-products, and election probabilities frequently are, as discussed above and in Kalshi's submission. For example, they can be used to help price economic event contracts. Investment banks provide clients and the public with recommendations on how Congressional outcomes affect macroeconomic forecasts. For example, Morgan Stanley cited the chance of stimulus along with infrastructure spending and corporate tax changes as a vehicle for a "blue wave" leading to a weaker dollar, lower interest rates, stronger GDP growth and lower bond prices.[9091] The Exchange provided many specific use cases and pricing analysis in its original submission.

Many also stated as much in public comments, including Flip Idiot, Victor Jacobsson, Angelo Lisboa, Peter Kempthorne, Seth Weinstein, David Pollard, David Trinh, Eriz Zitzewitz, James Cust, Caesar Tabet, Reed Newell, Jorge Paulo Lemann, Sebastian Strauss, Christopher Hehmeyer, Ron Conway, and Margaret Stumpp. As Stumpp, a senior vice president at Prudential Financial and a co-founder of Quantitative Management Associates, wrote,

> …a well functioning market for contingent political outcomes should improve the prices at which other securities (eg, stocks, bonds, options, etc…) trade. This reduces uncertainty, enhances capital market liquidity, and improves the efficiency by lowering uncertainty.[92]

Consider the following example: a junior investment bank has been instructed to price a security. That price is reflective of the stocks' net present value, itself a reflection of future expected profits. This includes political risk. If that banker knew with certainty that Republicans will take control of Congress, for example, and corporate taxes will not be raised, she would price the security higher than otherwise. Kalshi's contracts would help her in doing so.

14. Are the contracts contrary to the public interest? Why or why not?

No.

1: The contracts have a strong economic purpose.

The hedging and price basing use cases are myriad and would allow individuals to take advantage of a product that is currently strongly in demand. Elections cause extremely large

[90] Morgan Stanley. 2020. "A Revised Guide to Economic Policy Paths & Market Impacts".
[91] Morgan Stanley. 2020. "2020 US Election Preview: 5 Themes to Watch for Investors."
[92] Public comment by Margaret Stumpp. Available at https://comments.cftc.gov/PublicComments/ViewComment.aspx?id=69722.

economic impacts and are some of the biggest risks that many businesses will ever face. This is detailed at great length in Kalshi's submission and has been validated by dozens of public comments from retail, business, academia, and members of industry, including Kevin Standridge, Sam Altman, Geoff Ralston, Robert Orr, Valentin Perez, Robin Hanson, James Bailey, Rohan Palvulri, Jason Crwaford, Dustin Moskovitz, Andrew N, and James Angel.

2: The contracts would serve as useful tools for voters, the media, and the public that would fight disinformation, improve election integrity, and improve decision making including policy making

The demand for accurate information surrounding elections is enormous – and valuable. This is why so many Americans turn to election models and updates offered by *FiveThirtyEight*, *The New York Times*, and *The Economist* around election time for advanced models that incorporate information. Its markets are consistently referenced as informative and useful by major, credible news organizations like *CNN*, *CNBC*, *Politico*, *Bloomberg*, *The Economist*, *The Wall Street Journal*, *The Washington Post*, and *The New York Times*, across sections like *The Upshot*, *DealBook*, opinion columns, and the technology section. In addition, Predictit has repeatedly been cited by prominent political officials and thinkers. Examples include economists like Jason Furman, previously President Obama's Council of Economic Advisors Chair (who submitted a comment letter detailing election markets use while he was in the Administration); Nobel Laureate Paul Krugman, a Professor at The Graduate Center and a columnist for *The New York Times*; and data scientists/reporters like Nate Silver, founder and editor-in-chief of FiveThirtyEight.[93][94]

In a public comment, Furman also emphasized the importance of election markets for policy making. As he wrote,

> …in the White House I, along with other members of the economic team, would regularly refer to prediction markets on electoral outcomes and specific events to help inform our understanding of how political and economic developments would affect economic policymaking. In understanding the risks of a government shutdown or debt limit showdown, for example, it would be helpful to understand what informed traders with money at stake would expect—a method of understanding probabilities that research has consistently shown is superior to other ways of summarizing and updating based on information.[95]

[93] For the sake of brevity, a full list of citations in this section can be found at the end of this document.
[94] Public comment letter by Jason Furman. Available at: https://comments.cftc.gov/PublicComments/ViewComment.aspx?id=69708.
[95] *Ibid*

Professor Furman went on to detail the other benefits for the contract, including helping academic researchers and educational benefits, a point also made by others, including Sebastian Strauss. PredictIt also has been used to promote civic engagement by undergraduates. Berg and Chambers (2016) found that using prediction markets, including PredictIt, increased user interest in civics and user news consumption.[96]

The preponderance of the academic literature suggests that existing media has misaligned incentives when it comes to reporting on a given party's chances of political control. This often results in bad reporting. For example, University of Pennsylvania professor Philip Tetlock evaluated the statements made by pundits and found that 15 percent of predictions claimed to be "impossible" did indeed occur and 27 percent of predictions claimed to be a "sure thing" did not.[97]

By providing an instant check against pundits, a market-based price created by the contracts can aid information aggregation for the public. For the numerically-inclined or the financially-minded, a viewer can see that one commentator is asserting that candidate X is a "sure thing" but the Kalshi contract gives them only (e.g.) a 20% chance of winning. They now have a competing alternative to that pundit's information.

Markets tend to be more accurate than any pundit or forecasting alternatives. The efficient, price-discovering nature of markets in a wide range of contexts is a well-substantiated finding in academic research. The collective wisdom of many people who have a direct monetary stake in the outcome results in a valuable price signal. Weather derivatives and agricultural futures are better at predicting the weather than meteorologists. Markets trading on the reproducibility of scientific research are better at discovering which papers will reproduce than experts, who do no better than chance. Most importantly, research studying IEM and PredictIt have confirmed that markets provide more accurate information than traditional forecasting methods.

Kalshi's contracts would provide a visible, well-trusted benchmark against which to evaluate a pundit's predictive power. As Professor Tetlock observed, "prudent consumers should become suspicious" when they confront a public record of poor performance relative to the market. In Tetlock's words, "Unadjusted ex ante forecasting performance tells consumers in the media, business, and government what most want to know: how good are these guys in telling us what will happen next?"[98]

<u>3: The contracts would not serve as threats to either election integrity or the perception thereof; instead, it would improve them both.</u>

[96] Berg & Chambers. *Bet Out the Vote: Prediction Markets as a Tool to Promote Undergraduate Political Engagement*. 2018. Journal of Political Science Education.
[97] Philip Tetlock. "Expert Political Judgment". 2005.
[98] *Ibid*

Not threatening election integrity

It is important for the Commission to engage with the evidence on election integrity rather than speculate. The *Nadex Order's* suggestion that voters could be incentivized to switch their votes, and thus harm election integrity, was outright speculative in 2012, and has since been disproven by PredictIt's success without any claim of, let alone proof of, election impropriety driven by those markets. Today, election trading remains alive and well in other democracies like the United Kingdom, Australia, Ireland, and New Zealand[99], without documented attempts at–let alone successful–distortion of the electoral process. Several commenters confirmed this, including Eric Crampton, the academic advisor to iPredict, a New Zealand based political prediction market:

> What experience we had with iPredict suggests CFTC really doesn't have anything substantial to worry about in allowing contracts on political events. If anything, they heightened voter engagement. The CE [Chief Executive] of iPredict even featured on the nightly news during the election, giving the latest on election market prices. And for that brief period, whenever blowhard partisans insisted that some outcome was going to happen, people could just point to the iPredict price on the event and ask them why they thought that price was wrong, and whether they'd actually put their money where their mouth was. It was a remarkable era. iPredict inflation forecasts (they also had markets on inflation going out several years - it was so very good) wound up being noted in our Reserve Bank's Monetary Policy Statements. I desperately miss it. I envy the opportunities Americans could have if CFTC takes a sensible approach to regulation.[100]

Or Dustin Moskovitz, a co-founder of Facebook and founder of Asana:

> Of course, it's important to validate that these contracts would not conflict with the public interest, and specifically the integrity of our elections. I am confident, however, they would not do so. Similar markets not only exist in many liberal democracies like the UK, but create a thriving scene that actually encourages voter participation and engagement.[101]

References to other political markets without integrity issues were made by many commenters, including, in addition to the above, Justin Xavier Geraghty, Upsolve founder Rohan Pavuluri, People's Policy Project founder Matt Bruenig, Zvi Mowshowitz, Roots of Progress founder

[99] iPredict, the New Zealand political trading exchange, is no longer in operation, but was following the *Nadex Order*.
[100] Public comment by Eric Crampton. Available at https://comments.cftc.gov/PublicComments/ViewComment.aspx?id=69738.
[101] Public comment by Dustin Moskovitz. Available athttps://comments.cftc.gov/PublicComments/ViewComment.aspx?id=69716.

Jason Crawford, macro analyst Sebastian Strauss, Quantitative Management Associates co-founder Margaret Stumpp, and New York University Law School professor Max Raskin, among others.

The economic impacts of elections themselves dwarf the value of Kalshi's contracts many, many times over. Likely trillions in stock value are deeply dependent on elections; entire sectors, firms, and places can be favored by a candidate for office; and almost every actor in the economy is directly affected by tax rates. Elections already have billions in consequences for retail, small businesses, and industry, dwarfing the value of any Kalshi contract, and yet attempts at manipulation are unlikely, and successful manipulation even more so, thanks to the large, decentralized nature of elections, strong political norms, and laws protecting the vote. These contracts do not change, much less materially change the fact that individuals already have large stakes in election outcomes.

The only groups that can directly affect the leadership decisions are the U.S. Senate and U.S. House of Representatives. Members of these groups are extremely unlikely to attempt intentional manipulation of the leadership of their chambers merely to settle the contracts a certain way. Their finances are heavily monitored and subject to public disclosure and scrutiny, and Kalshi does not permit them, their close associates, or families to trade. Kalshi flags them and other politically exposed persons in the Know-Your-Customer authorization. Members of Congress also have a sworn duty to represent their constituents and have strong incentives not to manipulate electoral processes for private gain. Other related officials (like election officials, vote counters) also take such oaths and are heavily monitored because of the strong public interest in maintaining election integrity. This should clarify any claim that this could de-legitimize elections internal to Congress itself.

As further evidence, consider the history of political control contracts. University of Michigan professor Paul Rhode and Wake Forest professor Koleman Strumpf conducted a systematic review of the history of prediction markets both domestically and abroad, documenting their emergence back to "16th century Italy, 18th century Britain and Ireland, 19th century Canada and 20th century Australia and Singapore."[102][103] In the United States, they were popular from the post-Civil War period until the Great Depression tarnished the image of Wall Street in the public imagination. They wrote,

> Although vast sums of money were at stake, we are not aware of any evidence that the political process was seriously corrupted by the presence of a wagering market. This

[102] Paul Rhode and Koleman Strumpf. 2012. "The Long History of Political Betting Markets: An International Perspective." Strumpf also was a signatory to a supportive public comment. *See* Public comment 69735. Available at: https://comments.cftc.gov/PublicComments/ViewComment.aspx?id=69735&SearchText

[103] Paul Rhode and Koleman Strumpf. 2003. "Historical Prediction Markets: Wagering on Presidential Elections".

analysis suggests many current concerns about the appropriateness of prediction markets are not well founded in the historical record.[104]

Prices are not able to be manipulated to the give the false impression of momentum

One may also imagine that a coordinated group of individuals may conspire to manipulate market prices to give the false impression of candidate "momentum," thus potentially harming the democratic process. This concern has been tested several times by researchers, who have concluded that all attempts at manipulation have failed.

Koleman and Strumpf in a later paper examined previous American political prediction markets and found that no previous effort at manipulation was capable of sustaining anything more than fleeting price movements. They wrote, "we find little evidence that political stock markets can be systematically manipulated beyond short time periods."[105] Moreover, the markets examined were much smaller and thus even more prone to manipulation than a fully regulated, liquid market like a DCM. As a result, manipulation on Kalshi's market is even less plausible. Indeed, as George Mason University professor Robin Hanson and University of California at Santa Barbara professor Ryan Oprea found, one major reason why political contracts are resistant to manipulation attempts is that any attempt to manipulate prices induces informed counter-parties to enter on the other side of the market.[106] In fact, the greater the attempts to jack up one side's prices, the greater the returns to becoming an informed trader. As University of Michigan economist Justin Wolfers and Dartmouth economist Eric Zitzewitz wrote regarding previous political contracts, "none of these attempts at manipulation had a discernible effect on prices, except during a short transition phase."[107] This finding was also supported by over two dozen economists in their 2012 Nadex letter and by many letters supporting Kalshi's submission.[108][109]

Importantly, the fact that these contracts are already traded on Commission-sanctioned unregistered trading venues in the United States by Americans should demonstrate that they do not cause manipulation and that the markets are safe. In 2014, PredictIt, a new unregistered trading venue dedicated to election and political event contracts, received a no-action letter.

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[104] Paul Rhode and Coleman Strumpf. 2003. "Historical Prediction Markets: Wagering on Presidential Elections".
[105] Paul Rhode and Koleman Strumpf. 2005. "Manipulating Political Stock Markets: A Field Experiment and a Century of Observational Data."
[106] Robin Hanson and Ryan Oprea. 2008. "A Manipulator Can Aid Prediction Market Accuracy." *Economica*.
[107] Justin Wolfers and Eric Zitzewitz. 2006. "Prediction Markets in Theory and Practice".
[108] *Nadex* public comment by Zitzewitz et al. Available at https://www.cftc.gov/sites/default/files/stellent/groups/public/@rulesandproducts/documents/ifdocs/ericzitzewitzltr020312.pdf.
[109] For example, the public comment by David Rothschild and company. Available at: https://comments.cftc.gov/PublicComments/ViewComment.aspx?id=69735&SearchText=.

Since then, it has hosted more than $1B in contracts traded and has more than a quarter of a million registered users.[110]

This information – that hundreds of millions of dollars can be traded on political control contracts without triggering manipulation – was not available to the Commission the last time it considered similar event contracts in 2012. Although another political contract trading venue, the Iowa Electronics Market, received a no action letter in 1992, IEM is smaller and harder to access by individuals not associated with the University of Iowa. Now, far more money is known to have been traded on election outcomes.

The contracts would combat illegal behavior, improving the perception of election integrity

Americans can also readily access offshore platforms using a virtual private network such as Betfair.[111] Betfair had more than $500 million traded on the 2020 election.[112]These platforms are not registered with the Commission as DCMs, but frequently host such markets. There are no indications that the markets caused or induced an attempt to manipulate elections, let alone a successful manipulation. However, if the Commission is concerned that election markets could nevertheless create election integrity threats, it is imperative to shift trading to an exchange compliant with the Core Principles, with insider trading protections, surveillance, and KYC. In this way, among others, approving the contracts would improve, not harm, election integrity and the perception of it.

As part of the Exchange's KYC verification and monitoring system, the Exchange also cross-checks applicants against comprehensive databases. In particular, the Exchange will check whether any Members trading on these contracts are on databases of Politically Engaged Persons. The Exchange further cross checks applicants against databases of family members and close associates of Politically Engaged Persons. These checks help to further reduce the potential for trading violations and further increase the integrity of this Contract.

The contracts would promote the public perception in election integrity by providing an accurate and competing tool for election forecasting

As described in detail in the second part of this question's response, there is immense social value in accurate election forecasts. This will fight disinformation and promote truth with politics, increasing voter confidence and engagement.

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[110] LinkedIn profile of former PredictIt employee: "Oversaw company growth of nearly 400% - from roughly 50,000 registered users to more than 250,000 registered users, and over 1.2 billion shares traded on PredictIt's market exchange." https://www.linkedin.com/in/will-jennings-pi/

[111] Comment letter by policy commentator Matt Bruenig. Available at https://comments.cftc.gov/PublicComments/ViewComment.aspx?id=69670.

[112] See end of document.

Decreasing Partisanship

Studies consistently show that polarization and partisanship has increased dramatically in the last few decades: every year, greater numbers of people say they believe people from the opposite party are "immoral" and express other hostile sentiments. More concerning than mere hostility is how partisan antipathy can create alternative sets of facts--voters from different parties simply believe two sets of facts about the world. It is from this miasma where conspiracy theories about stolen elections emerge that damage the electoral process.

Prediction markets can help remedy this problem. Economists John Bullock, Alan Gerber, Seth Hill, Gregory Huber conducted an experiment in 2013 and found that partisan gap in beliefs (e.g. if Republicans believe a statement is true with probability 80%, and Democrats believe it with probability 35%, then the partisan gap is 45 percentage points) shrunk by a shocking 55 percent when participants were given a financial incentive for being right.[113] If they were given a lesser financial prize for answering "unsure" (versus none for being wrong and a greater amount for getting it correct), the gap shrunk by about 80 percent.

The reasoning roughly tracks as follows: when no money is at stake, people conflate their beliefs as preferences. For example, a highly partisan liberal may say that a Democratic Party candidate is definitely going to win the 2024 presidential elections this year (a belief), when in reality they merely want the Democrat to win the championship (a preference). However, that same individual when challenged to trade money on that "definite" prediction will re-evaluate and calculate the odds and decide whether or not they should take that trade. In short, when no money is at stake, people express beliefs as mere signaling, lending itself to heavy partisan bias. When money is at stake, they are able to differentiate their beliefs from their preferences. In other words, the partisan reality gap shrinks, and individuals who trade on election markets become more attune to facts and less to partisan groupthink.

In conclusion, the contracts are not contrary to the public interest; rather, it strongly supports the public interest, as demonstrated by the evidence above. The contracts will improve asset pricing, provide risk management opportunities, enhance election integrity and trust, and shift trading activity to regulated exchanges.

15. Could the trading of these or other political control or election-based contracts affect the integrity of elections or elections within a chamber of Congress? Could they affect the perception of the integrity of elections or elections within a chamber of Congress?

[113] John Bullock, Alan Gerber, Seth Hill, Gregory Huber. 2013. "Partisan Bias in Factual Beliefs about Politics."

No. The benefits that Kalshi's contracts will have on the electoral and political process, as well as reasons why it will not have a negative effect, are also discussed in the prior question's response. Many of those same arguments are repeated here for ease and clarity, organized to suit this question.

1: The contracts will not harm election integrity or the perception of election integrity

It is important for the Commission to engage with the evidence on election integrity rather than speculate. The *Nadex Order's* suggestion that voters could be incentivized to switch their votes, and thus harm election integrity, was outright speculative in 2012, and has since been disproven by PredictIt's success without any claim of, let alone proof of, election impropriety driven by those markets. Today, election trading remains alive and well in other democracies like the United Kingdom, Australia, Ireland, and New Zealand[114], without documented attempts at–let alone successful–distortion of the electoral process. Several commenters confirmed this, including Eric Crampton, the academic advisor to iPredict, a New Zealand based political prediction market:

> What experience we had with iPredict suggests CFTC really doesn't have anything substantial to worry about in allowing contracts on political events. If anything, they heightened voter engagement. The CE [Chief Executive] of iPredict even featured on the nightly news during the election, giving the latest on election market prices. And for that brief period, whenever blowhard partisans insisted that some outcome was going to happen, people could just point to the iPredict price on the event and ask them why they thought that price was wrong, and whether they'd actually put their money where their mouth was. It was a remarkable era. iPredict inflation forecasts (they also had markets on inflation going out several years - it was so very good) wound up being noted in our Reserve Bank's Monetary Policy Statements. I desperately miss it. I envy the opportunities Americans could have if CFTC takes a sensible approach to regulation.[115]

Or Dustin Moskovitz, a co-founder of Facebook and founder of Asana:

> Of course, it's important to validate that these contracts would not conflict with the public interest, and specifically the integrity of our elections. I am confident, however, they would not do so. Similar markets not only exist in many liberal democracies like the UK, but create a thriving scene that actually encourages voter participation and engagement.[116]

[114] iPredict, the New Zealand political trading exchange, is no longer in operation, but was following the *Nadex Order*.
[115] Public comment by Eric Crampton. Available at https://comments.cftc.gov/PublicComments/ViewComment.aspx?id=69738.
[116] Public comment by Dustin Moskovitz. Available athttps://comments.cftc.gov/PublicComments/ViewComment.aspx?id=69716.

References to other political markets without integrity issues were made by many commenters, including, in addition to the above, Justin Xavier Geraghty, Upsolve founder Rohan Pavuluri, People's Policy Project founder Matt Bruenig, Zvi Mowshowitz, Roots of Progress founder Jason Crawford, macro analyst Sebastian Strauss, Quantitative Management Associates co-founder Margaret Stumpp, and New York University Law School professor Max Raskin, among others.

The economic impacts of elections themselves dwarf the value of Kalshi's contracts many, many times over. Likely trillions in stock value are deeply dependent on elections; entire sectors, firms, and places can be favored by a candidate for office; and almost every actor in the economy is directly affected by tax rates. Elections already have billions in consequences for retail, small businesses, and industry, dwarfing the value of any Kalshi contract, and yet attempts at manipulation are unlikely, and successful manipulation even more so, thanks to the large, decentralized nature of elections, strong political norms, and laws protecting the vote. These contracts do not change, much less materially change the fact that individuals already have large stakes in election outcomes.

The only groups that can directly affect the leadership decisions are the U.S. Senate and U.S. House of Representatives. Members of these groups are extremely unlikely to attempt intentional manipulation of the leadership of their chambers merely to settle the contracts a certain way. Their finances are heavily monitored and subject to public disclosure and scrutiny, and Kalshi does not permit them, their close associates, or families to trade. Kalshi flags them and other politically exposed persons in the Know-Your-Customer authorization. Members of Congress also have a sworn duty to represent their constituents and have strong incentives not to manipulate electoral processes for private gain. Other related officials (like election officials, vote counters) also take such oaths and are heavily monitored because of the strong public interest in maintaining election integrity. This should clarify any claim that this could de-legitimize elections internal to Congress itself.

As further evidence, consider the history of political control contracts. University of Michigan professor Paul Rhode and Wake Forest professor Koleman Strumpf conducted a systematic review of the history of prediction markets both domestically and abroad, documenting their emergence back to "16th century Italy, 18th century Britain and Ireland, 19th century Canada and 20th century Australia and Singapore."[117][118] In the United States, they were popular from the

[117] Paul Rhode and Koleman Strumpf. 2012. "The Long History of Political Betting Markets: An International Perspective." Strumpf also was a signatory to a supportive public comment. *See* Public comment 69735. Available at: https://comments.cftc.gov/PublicComments/ViewComment.aspx?id=69735&SearchText

[118] Paul Rhode and Koleman Strumpf. 2003. "Historical Prediction Markets: Wagering on Presidential Elections".

post-Civil War period until the Great Depression tarnished the image of Wall Street in the public imagination.. They wrote,

> Although vast sums of money were at stake, we are not aware of any evidence that the political process was seriously corrupted by the presence of a wagering market. This analysis suggests many current concerns about the appropriateness of prediction markets are not well founded in the historical record.[119]

One may also imagine that a coordinated group of individuals may conspire to manipulate market prices to give the false impression of candidate "momentum," thus potentially harming the democratic process. This concern has been tested several times by researchers, who have concluded that all attempts at manipulation have failed.

Koleman and Strumpf in a later paper examined previous American political prediction markets and found that no previous effort at manipulation was capable of sustaining anything more than fleeting price movements. They wrote, "we find little evidence that political stock markets can be systematically manipulated beyond short time periods."[120] Moreover, the markets examined were much smaller and thus even more prone to manipulation than a fully regulated, liquid market like a DCM. As a result, manipulation on Kalshi's market is even less plausible. Indeed, as George Mason University professor Robin Hanson and University of California at Santa Barbara professor Ryan Oprea found, one major reason why political contracts are resistant to manipulation attempts is that any attempt to manipulate prices induces informed counter-parties to enter on the other side of the market.[121] In fact, the greater the attempts to jack up one side's prices, the greater the returns to becoming an informed trader. As University of Michigan economist Justin Wolfers and Dartmouth economist Eric Zitzewitz wrote regarding previous political contracts, "none of these attempts at manipulation had a discernible effect on prices, except during a short transition phase."[122] This finding was also supported by over two dozen economists in their 2012 Nadex letter and by many letters supporting Kalshi's submission.[123][124]

Importantly, the fact that these contracts are already traded on Commission-sanctioned unregistered trading venues in the United States by Americans should demonstrate that they do not cause manipulation and that the markets are safe. In 2014, PredictIt, a new unregistered

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[119] Paul Rhode and Coleman Strumpf. 2003. "Historical Prediction Markets: Wagering on Presidential Elections".
[120] Paul Rhode and Koleman Strumpf. 2005. "Manipulating Political Stock Markets: A Field Experiment and a Century of Observational Data."
[121] Robin Hanson and Ryan Oprea. 2008. "A Manipulator Can Aid Prediction Market Accuracy." *Economica*.
[122] Justin Wolfers and Eric Zitzewitz. 2006. "Prediction Markets in Theory and Practice".
[123] *Nadex* public comment by Zitzewitz et al. Available at https://www.cftc.gov/sites/default/files/stellent/groups/public/@rulesandproducts/documents/ifdocs/ericzitzewitzltr020312.pdf.
[124] For example, the public comment by David Rothschild and company. Available at: https://comments.cftc.gov/PublicComments/ViewComment.aspx?id=69735&SearchText=.

trading venue dedicated to election and political event contracts, received a no-action letter. Since then, it has hosted more than $1B in contracts traded and has more than a quarter of a million registered users.[125]

This information – that hundreds of millions of dollars can be traded on political control contracts without triggering manipulation – was not available to the Commission the last time it considered similar event contracts in 2012. Although another political contract trading venue, the Iowa Electronics Market, received a no action letter in 1992, IEM is smaller and harder to access by individuals not associated with the University of Iowa. Now, far more money is known to have been traded on election outcomes.

2: <u>It would improve election integrity and the perception of election integrity.</u>

It would also improve election integrity, and the perception thereof, by providing a useful tool for voters, the media, and the public that would fight disinformation and improve election integrity.

Shifting trading to a regulate house

Americans can also readily access offshore platforms using a virtual private network such as Betfair.[126] Betfair had more than $500 million traded on the 2020 election.[127]These platforms are not registered with the Commission as DCMs, but frequently host such markets. There are no indications that the markets caused or induced an attempt to manipulate elections, let alone a successful manipulation. However, if the Commission is concerned that election markets could nevertheless create election integrity threats, it is imperative to shift trading to an exchange compliant with the Core Principles, with insider trading protections, surveillance, and KYC. In this way, among others, approving the contracts would improve, not harm, election integrity and the perception of it.

As part of the Exchange's KYC verification and monitoring system, the Exchange also cross-checks applicants against comprehensive databases. In particular, the Exchange will check whether any Members trading on these contracts are on databases of Politically Engaged Persons. The Exchange further cross checks applicants against databases of family members and close associates of Politically Engaged Persons. These checks help to further reduce the potential for trading violations and further increase the integrity of this Contract.

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[125] LinkedIn profile of former PredictIt employee: "Oversaw company growth of nearly 400% - from roughly 50,000 registered users to more than 250,000 registered users, and over 1.2 billion shares traded on PredictIt's market exchange." https://www.linkedin.com/in/will-jennings-pi/

[126] Comment letter by policy commentator Matt Bruenig. Available at https://comments.cftc.gov/PublicComments/ViewComment.aspx?id=69670.

[127] See end of document.

Disrupting Disinformation

The preponderance of the academic literature suggests that existing media information has grossly misaligned incentives when it comes to reporting on a candidate's chances. These misinformed incentives tend to come from three sources: first, pundits may want to hype up a preferred candidate's chances in order to flatter the sensibilities of their audience. Second, pundits may want to directly contradict a so-called "mainstream" line about a candidate winning in order to gin up controversy and draw more clicks or viewership. As a result, they may claim an underdog is actually the true favorite and, to further court controversy and viewership, claim that evidence to the contrary is a function of fraud and deception. Third, even when pundits attempt to be honest, viewers themselves may seek out information that confirms their own biases, thus rewarding a subset of relatively dishonest commentators with greater advertising revenue from the increased viewership or readership. In fact, we have empirical evidence of the dismal performance of media figures in the science of prediction. University of Pennsylvania professor Philip Tetlock decided to evaluate the statements made by pundits to see if they bore a relationship to reality--they did not. 15 percent of statements claimed to be "impossible" did indeed occur and 27 percent of statements claimed to be a "sure thing" did not.[128]

How can transparent, regulated election prediction markets help to ameliorate this situation? By providing an instant check against the ability of pundits to assert specific outcomes are "likely" when in reality they are long-shots. For the numerically-inclined or the financially-minded, a viewer can see that one commentator is asserting that candidate X is a "sure thing" but the prediction markets give them only (e.g.) a 20% chance of winning, they now know to view that commentator with suspicion. Unless that individual gives compelling reasons why thousands of highly informed individuals with money at stake are all systematically wrong, a viewer can understand that the content they are receiving is ideologically motivated and adjust accordingly.

Markets tend to be more accurate than any pundit or forecasting alternatives. The efficient, price-discovering nature of markets in a wide range of contexts is an extremely well-substantiated finding in academic research. The collective wisdom of many people who have a direct monetary stake in the outcome results in an incredibly valuable price signal. Weather derivatives and agricultural futures are better at predicting the weather than meteorologists. Markets trading on the reproducibility of scientific research are much better at discovering which papers will reproduce than experts, who do no better than chance. Most importantly, research studying IEM and PredictIt have confirmed that election markets provide more accurate information than traditional methods.

[128] Philip Tetlock. "Expert Political Judgment". 2005.

By creating a visible, well-trusted benchmark against which to evaluate a pundit's predictive power, Tetlock writes, "prudent consumers should become suspicious" when they confront a public record of poor performance relative to the market. In Tetlock's words, "Unadjusted ex ante forecasting performance tells consumers in the media, business, and government what most want to know: how good are these guys in telling us what will happen next?"[129]

Considering how destructive the scourges of misinformation and fake news have become to our Republic--and how critical a role the media has played in amplifying that misinformation--the need for prediction markets as a potential check only grows. Indeed, we would contend that the benefit of election prediction markets on reducing misinformation is large.

Decreasing Partisanship

Studies consistently show that polarization and partisanship has increased dramatically in the last few decades: every year, greater numbers of people say they believe people from the opposite party are "immoral" and express other hostile sentiments. More concerning than mere hostility is how partisan antipathy can create alternative sets of facts--voters from different parties simply believe two sets of facts about the world. It is from this miasma where conspiracy theories about stolen elections emerge that damage the electoral process.

Prediction markets can help remedy this problem. Economists John Bullock, Alan Gerber, Seth Hill, Gregory Huber conducted an experiment in 2013 and found that partisan gap in beliefs (e.g. if Republicans believe a statement is true with probability 80%, and Democrats believe it with probability 35%, then the partisan gap is 45 percentage points) shrunk by a shocking 55 percent when participants were given a financial incentive for being right.[130] If they were given a lesser financial prize for answering "unsure" (versus none for being wrong and a greater amount for getting it correct), the gap shrunk by about 80 percent.

The reasoning roughly tracks as follows: when no money is at stake, people conflate their beliefs as preferences. For example, a highly partisan liberal may say that a Democratic Party candidate is definitely going to win the 2024 presidential elections this year (a belief), when in reality they merely want the Democrat to win the championship (a preference). However, that same individual when challenged to trade money on that "definite" prediction will re-evaluate and calculate the odds and decide whether or not they should take that trade. In short, when no money is at stake, people express beliefs as mere signaling, lending itself to heavy partisan bias. When money is at stake, they are able to differentiate their beliefs from their preferences. In other words, the partisan reality gap shrinks, and individuals who trade on election markets become more attune to facts and less to partisan groupthink.

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[129] *Ibid*

[130] John Bullock, Alan Gerber, Seth Hill, Gregory Huber. 2013. "Partisan Bias in Factual Beliefs about Politics."

Empowering Researchers and Policymakers

One of the most exciting applications of election event contracts is their ability to provide powerful new causal inference tools to researchers and policymakers. Right now, estimating the effect of elections is rather difficult--one cannot merely compare economic outcomes during one presidential administration versus another because the underlying conditions have dramatically changed. Likewise, comparing forward-looking financial indicators before and after Election Day runs into several problems, including that many markets are closed overnight and that the market has already priced in some probability of the eventual victor winning.

Enter political control contracts. If Party X has a 80 percent chance of winning and then when they actually win on election night, a stock goes up 1%, we can say that the total effect of the election was 5 percentage point (if going from 80 to 100 is 1%, then going from 0 to 100 is roughly 5%). But it can get even stronger: since researchers would now have a time series of how the probabilities change over time, they can use other events like debates, prominent speeches and the revelation of major scandals to regress forward-looking financial variables on election outcomes in a way impossible without prediction markets.

These tools are far from hypotheticals. Economists Justin Wolfers and Eric Zitzewitz have already conducted several studies that used previous prediction markets (like the Iowa Electronic Exchange) to discern the effects of political outcomes on economic variables.[131][132] However, the lack of liquidity on their underlying markets makes their studies relatively under-powered. Having a transparent, regulated exchange with greater liquidity could dramatically expand the universe of questions researchers could answer with this data.

Beyond researchers, a transparent, regulated exchange would create a large incentive for traders to develop sophisticated and accurate models about election outcomes in order to gain an edge. The 2016 and 2020 elections were famous for the failure of (most) published models, often attributed to systematic non-response bias in polls. A liquid prediction market would create an incentive for trading firms to develop solutions to these hard issues in order to make more money. Fortunately, there are substantial positive externalities to these investments: learning how better to model, poll and understand the population would help policymakers better understand their constituents so they can figure out what they actually want. Voting is a noisy signal of preferences--the financial incentive to create models to discern voter intentions could thus make our democracy even more responsive.

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[131] Erik Snowberg, Justin Wolfers and Eric Zitzewitz. "Partisan Impact on the Economy". *Journal of Economic Perspectives*. 2004.

[132] Erik Snowberg, Justin Wolfers and Eric Zitzewitz. "Party Influence in Congress and the Economy." 2006.

The demand for accurate information surrounding elections is enormous, and valuable. This is why so many Americans turn to election models and updates offered by *FiveThirtyEight*, *The New York Times*, and *The Economist* come election time for advanced models that incorporate information. On election night 2020, PredictIt's website crashed because of so much incoming traffic. Its markets being consistently referenced as informative and useful by major, credible news organizations like *CNN*, *CNBC*, *Politico*, *Bloomberg*, *The Economist*, *The Wall Street Journal*, *The Washington Post*, and *The New York Times*, across sections like *The Upshot*, *DealBook*, opinion columns, and the technology section. In addition, it has repeatedly been cited by prominent political officials and thinkers. Examples include economists like Jason Furman, previously President Obama's Council of Economic Advisors Chair (who submitted a comment letter detailing election markets use while he was in the Administration); Nobel Laureate Paul Krugman, a Professor at The Graduate Center and a columnist for *The New York Times*; and data scientists/reporters like Nate Silver, founder and editor-in-chief of FiveThirtyEight.[133][134]

16. Could the contracts be used to influence perception of a political party or its candidates' likelihood of success? To this end, could the contracts be used to manipulate fundraising or voting?

No. This concern has been tested several times by researchers on far smaller markets (which would be more susceptible to manipulation than a large, liquid market hosted by a regulated DCM) who have concluded that all attempts at manipulation have failed. The Commission should be evidence-based in its decision, though this also makes sense in theory.

Koleman and Strumpf examined American political prediction markets and found that no previous effort at manipulation was capable of sustaining anything more than fleeting price movements. They wrote, "we find little evidence that political stock markets can be systematically manipulated beyond short time periods."[135] Moreover, the markets examined were much smaller and thus even more prone to manipulation than a fully regulated, liquid market like one offered by a Designated Contract Market. As a result, manipulation on Kalshi's market is even less plausible. Indeed, as George Mason University professor Robin Hanson and University of California at Santa Barbara professor Ryan Oprea found, one major reason why political contracts are resistant to manipulation attempts is that any attempt to manipulate prices induces informed counter-parties to enter on the other side of the market.[136] In fact, the greater the attempts to push up one side's prices, the greater the returns to becoming an informed trader. As University of Michigan economist Justin Wolfers and Dartmouth economist Eric Zitzewitz wrote

[133] For the sake of brevity, a full list of citations in this section can be found at the end of this document.
[134] Public comment letter 69708. Available at: https://comments.cftc.gov/PublicComments/ViewComment.aspx?id=69708.
[135] Paul Rhode and Koleman Strumpf. 2005. "Manipulating Political Stock Markets: A Field Experiment and a Century of Observational Data."
[136] Robin Hanson and Ryan Oprea. 2008. "A Manipulator Can Aid Prediction Market Accuracy." *Economica*.

regarding previous political contracts, "none of these attempts at manipulation had a discernible effect on prices, except during a short transition phase."[137] This finding was also supported by over two dozen economists in their 2012 Nadex letter and by many letters supporting Kalshi's submission.[138][139]

This information–that billions of dollars have been traded on contemporary political control contracts without triggering manipulation–was not available to the Commission the last time it considered similar event contracts in 2012. Although another political contract trading venue, the Iowa Electronics Market, received a no-action letter in 1992, IEM is smaller and harder to access by individuals not associated with the University of Iowa. Now, far more money is known to have been traded on election outcomes without any adverse consequences.

Almost all claims that this is a possible threat are unsubstantiated, though the letter provided by Dennis Kelleher of Better Markets does try to provide some evidence. Specifically, it argued:

> The proposed event contract is readily susceptible to manipulation… In her 2009 Harvard Law Review article "Prediction Markets and Law: A Skeptical Account," Professor Rebecca Haw Allensworth detailed how bad actors might manipulate prediction markets: 'Prediction markets are vulnerable to manipulation…First, they could profit by artificially lowering the trading price temporarily and purchasing shares to be sold at a higher price when the market returns to 'normal'. Second, they could try to affect the informational value of the market. For example, a candidate's supporter could purchase his shares at an inflated value, raising the perceived odds that he would win the election, and (hopefully) getting more voters to jump on the putative bandwagon'.[140]

There are several issues with this line of reasoning:

1. Critically, this is a misapplication of the cited research.
    a. Allensworth only cites one incident of successful manipulation, on an online exchange called TradeSports, referencing the case study on the incident conducted by Paul W. Rhode & Koleman S. Strumpf's, "Manipulating Political Stock Markets: A Field Experiment and a Century of Observational Data." However, Rhode and Strumpf conclude the opposite of Allensworth/Better Markets: that even the attempt to manipulate TradeSports' small, unregulated market only succeeded in changing prices briefly, and conclude, "In the cases studied here, the speculative attack initially moved prices, but these changes were quickly undone and prices returned close to their previous levels. We find little evidence that

[137] Justin Wolfers and Eric Zitzewitz. 2006. "Prediction Markets in Theory and Practice".
[138] *Nadex* public comment by Zitzewitz et al. Available at https://www.cftc.gov/sites/default/files/stellent/groups/public/@rulesandproducts/documents/ifdocs/ericzitzewitzltr020312.pdf.
[139] For example, the public comment by David Rothschild and company. Available at: https://comments.cftc.gov/PublicComments/ViewComment.aspx?id=69735.
[140] Public Comment by Dennis Kelleher. Available at: https://comments.cftc.gov/PublicComments/ViewComment.aspx?id=70788

political stock markets can be systematically manipulated beyond short time periods."

b. The other study cited, by Deck et al., does find researchers successfully manipulate a small exchange of *their own creation, with made up assets, with a mere eight traders*. This clearly cannot be grounds to judge Kalshi's proposed contracts.

2. The vast majority of research on this issue demonstrates how shockingly resilient such markets are to manipulation even in spite of no regulation. This is discussed at length also in Appendix G, which details how the Contract is in compliance with Core Principle 3.
    a. Like Allenworth, Deck et al. acknowledge this.[141] They wrote, "Wolfers and Zitsewitz (2004, p. 119) assert that 'The profit motive has usually proven sufficient to ensure that attempts at manipulating these [prediction] markets were unsuccessful.' Failed attempts at manipulating markets include political candidates betting on themselves (Wolfers and Leigh 2002) and bettors placing large wagers at horse races (Camerer 1998). Hansen, et al. (2004) did successfully manipulate election prediction markets, but the effects were short lived. In fact, Rhode and Strumph (2009, p. 37) provide an extensive discussion of attempts to manipulate political markets and conclude that 'In almost every speculative attack, prices experienced measurable initial changes. However, these movements were quickly reversed and prices returned close to their previous levels.'" They go on to cite more experiments that showed resilience to manipulation, including that of Ryan Oprea and Robin Hanson, two supportive commenters.[142] They do not find any research that shows any successful manipulation that is not short-lived.
3. The research cited by Better Markets only focused on small-scale, generally illiquid, unregulated online prediction markets. A highly regulated market that can onboard institutional clients is even less likely to be a victim of a particular manipulator, as markets incentivize speculators to reverse any potential price impact a manipulator could have. Indeed, Hanson and Oprea found, one major reason why political contracts are resistant to manipulation attempts is that any attempt to manipulate prices induces informed counter-parties to enter on the other side of the market. In fact, the greater the attempts to jack up one side's prices, the greater the returns to becoming an informed trader. As University of Michigan economist Justin Wolfers and Dartmouth economist Eric Zitzewitz wrote regarding previous political contracts, "none of these attempts at manipulation had a discernible effect on prices, except during a short transition phase." This finding was also noted by over two dozen economists in their 2012 Nadex letter and by many letters supporting Kalshi's submission.

[141] Deck, C., Lin, S., & Porter, D. (2010). Affecting policy by manipulating prediction markets: Experimental evidence. ESI Working Paper 10-17.
[142] Hanson, R. and Oprea, R. "A Manipulator Can Aid Prediction Market Accuracy," Economica, 2009, 76, 304-314.

17. Could the contracts facilitate violations of, or otherwise undermine, federal campaign finance laws or regulations? For example, could the contracts make it easier to sidestep prohibitions governing coordination between candidate campaign committees and political action committees?

No. The concerns this question raises are completely unrelated to the contract's function or impact. It would not improve (or impact at all) the ability of PACs and campaigns to coordinate.

If the implication is that they could do so more easily by providing an accurate picture of the state of the race, then public polling would also help such parties sidestep federal law, a plainly untenable proposition.

As described earlier, it is not plausible for any actor to try and create 'momentum' for their party by buying up one side's shares. One may also imagine that a coordinated group of individuals may conspire to manipulate market prices to give the false impression of candidate "momentum", thus potentially harming the democratic process. This concern has been tested several times by researchers, with all attempts failing. Koleman and Strumpf in a later paper examined previous American political prediction markets and found that no previous effort at manipulation were capable of sustaining anything more than fleeting price movements. They wrote, "we find little evidence that political stock markets can be systematically manipulated beyond short time periods."[143] Moreover, the markets examined were much smaller and thus even more prone to manipulation than a fully regulated, liquid market like a DCM. As a result, the probability of manipulation is implausible. Indeed, as George Mason University professor Robin Hanson and University of California at Santa Barbara professor Ryan Oprea found in one paper, one major reason why political contracts are rather invulnerable to manipulation attempts is that any attempt to manipulate prices induces informed counter-parties to enter on the other side of the market.[144] In fact, the greater the attempts to increase one side's prices, the greater the returns to an informed trader. As University of Michigan economist Justin Wolfers and Dartmouth economist Eric Zitzewitz write regarding previous political contracts, "none of these attempts at manipulation had a discernible effect on prices, except during a short transition phase."[145] This finding was also supported by the 2012 Nadex letter by over two dozen economists in the field and many of the ones supporting Kalshi's submission.[146][147]

[143] Paul Rhode and Koleman Strumpf. 2005. "Manipulating Political Stock Markets: A Field Experiment and a Century of Observational Data."
[144] Robin Hanson and Ryan Oprea. 2008. "A Manipulator Can Aid Prediction Market Accuracy." *Economica*.
[145] Justin Wolfers and Eric Zitzewitz. 2006. "Prediction Markets in Theory and Practice".
[146] *Nadex* public comment by Zitzewitz et al. Available at https://www.cftc.gov/sites/default/files/stellent/groups/public/@rulesandproducts/documents/ifdocs/ericzitzewitzltr020312.pdf.
[147] For example, the public comment by David Rothschild and others. Available at: https://comments.cftc.gov/PublicComments/ViewComment.aspx?id=69735&SearchText=.

18. Do the contracts present any special considerations with respect to susceptibility to manipulation or surveillance requirements?

As discussed at length in other parts of this letter, Kalshi's contract is not readily susceptible to manipulation, and is outright less susceptible than other commodity futures contracts. Kalshi engages in extensive market surveillance and employs Know-Your-Customer authorization to prevent manipulation in compliance with the Core Principles. Accordingly, we believe the contemplated measures combined with Kalshi's robust market surveillance program and dedicated technology are appropriately calibrated to address the particular risks associated with these particular contracts. Kalshi's rules also prohibit trading on non-public material information.

As with other contracts that deal with publicly important information, such as on the monetary policy decisions of the Federal Reserve, the integrity of the decision-making process by the Federal Open Market Committee has not been eroded despite contracts that trade enormous volumes on their impact. This is no different.

For these contracts, Kalshi employs Know-Your-Customer authorization and would prevent trading by Politically Exposed Persons, including campaigns and PACs, as well as operator's close associates and family. It also has identified a long list of political actors who are specifically prohibited from trading.

Regarding informational advantages of market participants and private polling, a privately commissioned poll is not materially non-public information; any market actor can employ similar research strategies in many other markets. Every market has a discrepancy between its trading members' resources. For example, hedge funds have access to Bloomberg terminals that retail investors can't afford. Market participants have a financial incentive to gain access to better information; entire teams of meteorologists are hired to accurately predict agricultural futures prices. As then Commissioner Quintenz explained, "The goal of financial markets is not to protect or shelter the less informed. Rather, the market incentivizes being informed and executing on that knowledge. In other words, market efficiencies are earned - they are created through research, investment, and intellectual property."[148] This is a benefit of listing a market, not a harm; it results in more accurate pricing for the market, the benefits of which are discussed in detail in the questions regarding public interest.

Further, there are robust protections against manipulation. The Exchange has rules that prohibit manipulative trading, and the Exchange performs surveillance to detect manipulation. This serves as a deterrent to attempts to manipulate the market via manipulative trading. In addition, the Exchange's rules also prohibit trading on non-public information, and the Exchange performs

[148] See Statement of Commissioner Brian D. Quintenz on the Certification of ICE Futures U.S., Inc. Submission No. 19-119, May 15, 2019. Available at: https://www.cftc.gov/PressRoom/SpeechesTestimony/quintenzstatement051519

surveillance to detect violations of this rule. The Exchange is also adopting contract specific gating rules that further buttress this rule. Specifically:

a. Before being allowed to participate, market participants must certify that they are not implicated by the prohibition list in Appendix B
b. Before being allowed to participate, market participants must certify that they do not have access to material nonpublic information
c. The Exchange's surveillance staff will conduct manual background checks and interviews with the top traders in a market, as well as randomly selected participants, to monitor and enforce the gating rules

The Exchange will be surveilling its market for any sign of trading that is indicative of manipulative or fraudulent behavior. The Commission will have all of the necessary data to do the same, should it so wish.

As discussed at length earlier in this response and in Kalshi's original filing, American elections are not readily susceptible to manipulation. In fact, manipulation of which party controls the U.S. Congress has never occurred. This is in contrast to existing markets that the CFTC regulates. Indeed, the CFTC has brought numerous enforcement actions against market participants who either manipulated or attempted to manipulate markets in oil, precious metals, cattle, and other commodity spot and futures markets. The Commission regularly brings almost a hundred enforcement actions per year and orders billions in monetary relief. Then, of course, there are digital asset markets, where the Commission has brought dozens of actions in an incredibly short time. Contrast that with elections, where election or voter fraud is extremely rare, and never succeeds at flipping the outcome of which party controls Congress. Even in cases where election manipulation has been attempted, it has only succeeded in affecting extremely small, local elections.[149]

Any attempt to manipulate the contract would most certainly involve a high degree of speculation; the contract is in regard to the sum of hundreds of elections. It is not even possible to determine which elections will be the closest (and thus easiest to affect) in advance, even if some races are understood to be more close than others. As detailed in Appendix F, a large-scale conspiracy to coerce many individuals to vote a particular way across many different jurisdictions without being detected. A fraud of sufficient size would mean that this fraud is no *Ocean's 8*, or even *Ocean's 11*. You'd be looking at Ocean's-well-into-the-hundreds-if-not-hundreds-of-thousands. Manipulation of polling machines themselves is equally quixotic.[150] Taken all in all, it is very unlikely that a fraud pertaining to this contract will be attempted, and considerably less likely than in other areas that fall under the Commission's enforcement authority.

[149] https://www.brennancenter.org/our-work/research-reports/truth-about-voter-fraud
[150] https://www.washingtonpost.com/politics/2022/11/01/truth-about-election-fraud-its-rare/

Critically, there are already enormous stakes in U.S. elections, creating incentives for outcome manipulation; this contract will not change that fact. As discussed in extensive detail in Appendix B, in the public comments, and to anyone involved in industry, elections move prices and it is specious to presume that they do not. Wall Street firms and global finance all trade elections. The contract before the Commission is not novel in that regard; rather, it is a more efficient instrument than what firms currently use to take positions on elections.

19. What is the price forming information for these contracts while the contracts are trading? If the price forming information includes polling and other election prediction information, is that information regulated? How does the price forming information compare to informational sources (e.g. government issued crop forecasts, weather forecasts, federal government economic data, market derived supply and demand metrics for commodities, market-based interest rate curves, etc.) that are generally used for pricing commodity derivative products within the Commission's jurisdiction?

There is a plethora of information used by the public and market participants to help calculate the probability that a given party will take control of Congress. Some of these are regulated (e.g. federal government economic data) but some are not (e.g. polls). That being said, there is no requirement that such information be regulated, nor is it clear that regulated information is the primary source of pricing information for many commodity futures contracts compared to private market forecasts and data. As discussed at other points in this response, demand for accurate information on election probabilities is in incredibly high demand by the public, and as a result, there is a large, competitive market for such content.

With regard to whether polling would become regulated, the answer is not any more or any less than any of the other information that goes into pricing any commodity.

20. Should, and if so how would, the registered entity listing the contracts take steps to address possible manipulative and/or false reporting activity involving the price forming information for the contracts, while the contracts are trading?

The Exchange has already taken great steps to prevent and address manipulative behavior. As in some of the prior questions, it seems odd for the Commission to request *only* the public's input in this regard, but has not discussed this with Kalshi. Regardless, the Exchange has numerous safeguards in place to prevent manipulation.

Additionally, the Exchange notes that in particular, concerns regarding manipulating this contract are broadly unlikely. The market for credible information on elections and their probabilities is very competitive, and false information is equally as likely to impact Kalshi's market as reports regarding the production of oil do for oil futures. Should false information be reported, the

returns from being an informed trader who could sniff out so much information would grow commensurately.

That being said, the Exchange nonetheless is extremely focused on making sure that such concerns would not affect the market. For example, it has gated out polling organizations, and employees thereof, from trading. Kalshi engages in extensive market surveillance and employs Know-Your-Customer authorization to prevent manipulation in compliance with the Core Principles. The contemplated measures combined with Kalshi's robust market surveillance program and dedicated technology are appropriately calibrated to address the particular risks associated with these particular contracts. Kalshi's rules also prohibit trading on non-public material information.

As with other contracts that deal with publicly important information, such as on the monetary policy decisions of the Federal Reserve, the integrity of the decision-making process by the Federal Open Market Committee has not been eroded despite contracts that trade enormous volumes on their impact. This is no different.

It is also important to note what the correct legal standard is, which is not "free from attempted manipulation." Indeed, one need only to peruse the annals of the CFTC's enforcement actions to find many contracts that were manipulated (e.g. LIBOR) or the subject of an attempted manipulation. These event contracts, such as oil contracts, interest rate swaps, etc. are significantly more likely and susceptible to be manipulated than this contract. Indeed, the fact that a contract like this on a regulated market is so unlikely to be manipulated successfully is one of the reasons that the public is so keen on seeing the data from the market which will be far more reliable than many other data sources currently available.

21. Do Kalshi's limitations on market participation affect the susceptibility of the contracts and/or markets for the contracts to manipulation? Do the limitations affect the extent to which these markets could be used to influence perception of a political party or candidate or otherwise be implicated in attempted election manipulation? Are the limitations reasonably enforceable?

In practice, few to no parties have access to material insider information on the contract's outcome. Any potential information an actor could have is highly unlikely to be material regarding the outcome of–in total–several hundred Congressional races. It is important to keep in mind that the argument that Congressional Control can come down to the outcome of a handful of races, and some races can be decided by a margin of several thousand, hundred, or even individual votes, has little to no bearing on the contract's susceptibility to manipulation. The margin of victory before an election is unknown. If a nefarious actor attempted to manipulate the election in order to manipulate the contract, which is what the CFTC is asking in this question,

the actor would not know beforehand what the margin of victory would be. That nefarious actor would have to assess the size of the electorate, which is in every instance going to be large. Accordingly, it is hard to conceive of the definitive piece of material non-public information that will swing the outcome of the contract.

However, like all contracts on Kalshi, there is a prohibition to trade on material nonpublic information. This contract is no different in that regard. In response to various indications from the Commission, however, the Exchange adopted contract-specific rules for this contract to gate out certain people who would be more likely to have information that could be considered material nonpublic information. This gating itself is the proverbial "safeguard on a safeguard".

As in other questions, Kalshi notes the incongruity of asking the public for input on how Kalshi will enforce a rule, without having asked Kalshi. Regardless, this rule is enforceable.

22. Should the Commission be responsible for surveilling, and enforcing against, possible manipulative and/or false reporting activity involving the price forming information for the contracts, while the contracts are trading?

It should be responsible for surveilling and enforcing against manipulative and false reporting activity while the contracts were live as much as it is responsible for doing so with other listed contracts, no more, no less.

Further, the Exchange notes that one of the benefits of having this activity on a regulated exchange is that the Commission will, for the first time, gain insight into the amount and level of activity of trading on congressional control. Currently, if, for example, Congress would invite the CFTC to the Hill and ask the CFTC to describe the current financial activity on congressional control, the CFTC will have nothing to say beyond there is activity, some on OTC, some on unregulated markets, some overseas. When pressed for details on who is participating, the CFTC will have to confess its utter ignorance. However, if the contract were to trade on regulated exchanges, the CFTC will not only know precisely what positions are being taken on the regulated markets, they will know who is taking them.

23. Could trading in the markets for the contracts obligate the Commission to investigate or otherwise become involved in the electoral process or political fundraising? If so, is this an appropriate role for the Commission?

There is no reason for the Commission to believe it will be responsible for policing attempts at, or successful, election fraud. No more and no less than the CFTC is responsible for any other type of underlying fraud that has impacts on a contract. Earlier this year, there were two individuals who were arrested for attempting to destroy power stations with the ultimate goal of

destroying the city of Baltimore.[151] If successful, the sabotage would have impacted electricity prices significantly. Is the CFTC "obligated . . . to investigate or otherwise become involved in the" prosecution of these two individuals? Is the CFTC "obligated . . . to investigate or otherwise become involved in the" protecting of America's power grid? OPEC+ impacts the prices of global oil, including the futures markets that the CFTC regulates. Is the CFTC therefore "obligated . . . to investigate or otherwise become involved in the" OPEC+ meetings? Is the CFTC "obligated . . . to investigate or otherwise become involved in the" determination of corporate dividends that underlie the CME's contract? The answer to all of these is that the CFTC will get involved to the extent that it is necessary for it to administer and enforce the CEA. The CFTC does not, in any of these cases, assume the role of the "cop on the beat". This application here is no different.

Election manipulation is a crime.[152] There are law enforcement agencies who police elections, and elections are policed much more effectively than other markets that have CFTC derivative products trading on them. The Commission is not the only "cop on the beat" with regard to election fraud. Elections, unlike many other reference markets or events that have CFTC-derivatives trading on them, are governed by multiple law enforcement agencies whose very existence is to prevent and detect election manipulation and fraud. This includes the Federal Election Commission, the federal Department of Justice, state election commissions, state Secretaries of State, and state ethics commissions. History has shown that these agencies are very good at their job. The other day, the CFTC brought an enforcement charge against Alexander Mashinsky and Celsius Network, LLC, where the CFTC acknowledged the role that was played by both the SEC and the U.S. Attorney's Office for the Southern District of New York.[153] Similarly, Cody Easterday committed fraud that was discovered by Tyson foods and prosecuted by the Department of Justice. The CFTC *also* charged Easterday, presumably after cooperating with the relevant criminal authorities. These are two examples of many. The CFTC is well-versed in cooperating with the relevant law enforcement agencies, be it the FBI or DOJ or any other relevant federal or state authority. There is no reason to assume that the CFTC would somehow lose that competency in this case.

24. What other factors should the Commission consider in determining whether these contracts are "contrary to the public interest?"

The Commission has never fully defined the full extent of the factors it considers under the public interest standard in Section 5c(c)(5)(C). Even the Nadex Order admits that the Commission can consider factors other than the economic purpose test. The Commission is not an expert in all areas, such as election law or integrity, voter confidence, or how to foster

[151] https://abc7chicago.com/power-grid-attack-sarah-clendaniel-brandon-russell-baltimore-plot/12777303/.
[152]https://www.fbi.gov/how-we-can-help-you/safety-resources/scams-and-safety/common-scams-and-crimes/election-crimes-and-security#:~:text=Intentionally%20deceiving%20qualified%20voters%20to,%2Fhow%2Dto%2Dvote.
[153] https://www.cftc.gov/PressRoom/PressReleases/8749-23

democracy, and the Commission should instead focus on what it knows: the value of a contract as a hedging interest and the value of a contract's price to market participants. As we noted in response earlier, these contracts are not contrary to the public interest because they have a large economic purpose, would serve as a useful tool for voters, the media, and the public that would fight information and improve election integrity. We note that the evidence supporting the contracts is wholly consistent with the stated findings and purpose of the CEA found in 7 USC 5. The contracts provide "a means for managing and assuming price risks, discovering prices, or disseminating pricing information through trading in liquid, fair and financially secure trading facilities."[154] These contracts and their trading on Kalshi would "protect all market participants from fraudulent or other abusive sales practices and misuses of customer assets."[155] Finally, allowing these contracts to trade on a CFTC-regulated DCM would "promote responsible innovation and fair competition among boards of trade, other markets and market participants."[156] In sum, these contracts are consistent with the CEA and its purposes and Kalshi has shown that they should be traded on a CFTC-regulated exchange with all of the protections that the CEA makes available to market participants.

The Commission should hold a contract is contrary to the public interest if it:

- Has no economic purpose
- Has no hedging utility;
- Has no price basing utility - meaning it has no effect on the prices of other commodities, assets, services, or commodity interests, which must therefore include *affecting the probabilities of* other events on which event contracts are now or in the future trading.
- *And* has no forecasting value to the public.

[154] 7 USC 5(a).
[155] 7 USC 5(b).
[156] *Ibid*